Postal Regulatory Commission
Submitted 2/2/2017 3:15:03 PM
Filing ID: 98896
Accepted 2/2/2017

BEFORE THE
POSTAL REGULATORY COMMISSION
WASHINGTON, DC 20268-0001

Annual Compliance Review, 2016 | Docket No. ACR2016

PUBLIC REPRESENTATIVE COMMENTS
(February 2, 2017)

Respectfully submitted,

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I. INTRODUCTION

Pursuant to the Commission's Notice,[1] the Public Representative hereby comments on the Postal Service's FY 2016 Annual Compliance Report (FY 2016 ACR) filed for fiscal year 2016 as prescribed by the Postal Accountability and Enforcement Act (PAEA).[2]

The Postal Service's FY 2016 ACR is "to demonstrate that all products during the year complied with all applicable requirements of [title 39]." 39 U.S.C. § 3652(a)(1). The Public Representative has reviewed the Postal Service's FY 2016 ACR together with previous Commission Annual Compliance Determinations (ACDs) and the Commission's directives and recommendations for Postal Service action in those proceedings. These comments address matters relating to the Postal Service's (1) service performance, (2) customer satisfaction, (3) market dominant products, (4) worksharing, and (5) competitive products.[3]

Section II of these comments addresses the Postal Service's FY 2016 service performance results. The Public Representative concludes that the recent service performance decline has stabilized and service has started to recover. However, most

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[1] Notice of Postal Service's Filing of Annual Compliance Report and Request for Public Comments, Order No. 3717, December 30, 2016 (Order No. 3717).

[2] United States Postal Service FY 2016 Annual Compliance Report, December 29, 2016 (FY 2016 ACR); *see* 39 U.S.C. § 3652.

[3] Comments on the Postal Service's strategic initiatives and performance plans required by 39 U.S.C. § 2803 and § 2804 are deferred to a time to be determined by a forthcoming Commission notice regarding the Postal Service's FY 2016 Performance Report and FY 2016 Performance Plan. *See* Order No. 3717 at 2, n.2.

service performance levels remain below the applicable targets. The Public Representative urges the Commission to continue taking an active role in driving improvement in this area. The Public Representative again asks the Commission to consider the implementation of a new metric, “actual calendar days to delivery.” This may provide better insight into actual service performance.

Section III of these comments addresses the Postal Service’s FY 2016 customer satisfaction results. The Public Representative makes the following conclusions. Wait-time-in-line results have slightly increased, but are in the acceptable range. The results of the customer satisfaction surveys show a decline in customer satisfaction. The number of collection boxes continues to decline further reducing customer access. Not much progress has been made in resolving the post office suspension issue.

Section IV of these comments addresses the Postal Service’s FY 2016 market dominant statutory requirements. A focus of the comments is on whether or not products cover attributable costs. The Public Representative concludes that at least nine market dominant products are underwater, equaling approximately $1.390 billion in lost revenues. This is greater than an 11 percent increase compared with the previous year.

Section V of these comments addresses the Postal Service’s FY 2016 worksharing statutory requirements. The Public Representative focuses on thirty-three First-Class Mail, Standard Mail, and Package Service worksharing passthroughs that exceed 100 percent. The Public Representative urges the Commission to require the Postal Service to provide more substantial justification in the future for the excessive passthroughs. The Public Representative also asks the Commission to address the systemic timing problem of reviewing worksharing passthroughs relative to costs that were developed at another time. This problem makes it impossible to determine compliance with the statutory requirements.

Section VI of these comments addresses the Postal Service’s FY 2016 competitive products requirements. The Public Representative concludes that the competitive products statutory requirements are generally met. However, there are at least four international products and 13 domestic Negotiated Service Agreements that did not cover attributable costs.

II. SERVICE PERFORMANCE

A. Introduction

The Postal Service is required to annually report the level of service achieved by each market dominant product (in terms of speed of delivery and reliability). 39 U.S.C. § 3652(a)(2)(B)(i). Whether or not the level of service achieved is in compliance with the applicable service standards is determined by comparing the actual level of service against service targets (goals) established by the Postal Service. Based upon this comparison, the Commission then makes an annual determination of whether or not individual market dominant products were in compliance with the service standards in effect during such year. 39 U.S.C. § 3653(b)(2).

The encouraging news is that, in most instances, service performance levels have recovered from last year's drop in service performance. However, most service performance levels remain below the applicable targets.

The Postal Service reports that not one First-Class Mail product met its service performance target for the second year in a row. Within Standard Mail, the Postal Service reports that only High Density and Saturation Letters, and Parcels, exceeded service performance targets. High Density and Saturation Flats/Parcels, Carrier Route, Letters, Flats, and Every Door Directs Mail-Retail fell below service performance targets. The Postal Service reports that both Periodicals products failed to meet service performance targets in FY 2016. The Postal Service reports that within Package Services, Bound Printed Matter Parcels and Media Mail/Library Mail met their service performance targets in FY 2016. However, Bound Printed Matter Flats only met its service performance standard 53.6 percent of the time, which is 36.4 percent below target. The Postal Service reports that most Special Services, except for Post Office Box Service, exceeded their service performance targets.

The Public Representative is discouraged by the lack of visibility (any plan) that the Postal Service provides in its FY 2016 ACR as to how it is going to achieve service performance goals in the future. This would not be an issue if it were not for the fact that the majority of service performance targets are not being met, and except for this year's recovery (essentially to prior levels) service performance does not appear to be improving over time. The Postal Service typically provides only one or two line statements indicating why service performance levels are not being achieved or what actions are being taken. In the opinion of the Public Representative, those statements are wholly insufficient given the lack of observable improvement. Thus, the Public Representative urges the Commission to continue, if not increase, its efforts of directing the Postal Service to improve service performance for all market dominant products.

Reported service performance for each class of market dominant mail is discussed below. This is followed by the Public Representative's suggestions for action that the Commission might consider to drive improvement in market dominant service performance.

B. First-Class Mail

Generally, FY 2016 First-Class Mail service has improved compared to the service provided in the previous year. With the exception of Outbound Single-Piece First-Class Mail International two-day mail, all overnight and two-day categories show some improvement. The three-to-five day reporting categories across all First-Class Mail products show significant improvement. For the three-to-five day reporting categories, the improvements may mean that the Postal Service has been successful in addressing related transportation and processing issues. Overall, this is positive news, which demonstrates that the Postal Service is recovering from the service performance issues most likely attributable to its network realignment initiatives.

However, for the second year in a row, none of the First-Class Mail products met service performance targets (for FY 2015 or FY 2016). Furthermore, except for First-Class Mail Parcels two-day, none of the First-Class Mail products have recovered to the service performance levels observed in FY 2014. This suggests that the Postal Service has more work to do and that the Commission should continue its efforts to improve service performance.

Table II-1 (domestic First-Class Mail products) and Table II-2 (International First-Class Mail products) compare the First-Class Mail annual targets and percent on-time performances for FY 2014 through FY 2016.

Table II-1
Domestic First-Class Mail Annual Targets and Percent On-Time
FY 2014 through FY 2016

First-Class Mail	Annual FY 2014[1]		Annual FY 2015[2]		Annual FY 2016[3]	
	Target (%)	On-Time (%)	Target (%)	On-Time (%)	Target (%)	On-Time (%)
Single-Piece Letters/Postcards						
Overnight	96.80	96.7	96.80	95.8	N/A	N/A
Two-Day	96.50	95.7	96.50	94.0	96.50	95.5
Three-To-Five-Day	95.25	88.6	95.25	77.3	95.25	84.8
Presort Letters/Postcards						
Overnight	96.80	97.2	96.80	96.0	96.80	96.3
Two-Day	96.50	96.6	96.50	93.8	96.50	95.2
Three-To-Five-Day	95.25	92.5	95.25	88.0	95.25	91.9
Flats						
Overnight	96.80	84.9	96.80	83.2	96.80	84.5
Two-Day	96.50	82.5	96.50	79.8	96.50	80.6
Three-To-Five-Day	95.25	72.6	95.25	65.3	95.25	70.9
Parcels						
Overnight	96.80	88.4	96.80	84.8	96.80	N/A
Two-Day	96.50	86.8	96.50	84.2	96.50	88.7
Three-To-Five-Day	95.25	83.8	95.25	73.7	95.25	80.3
Exceeded Target by:	≥0%					
Missed Target by:	>0-5%	5-10%	10-15%	15-20%	>20%	

[1] Library Reference USPS-FY14-29, Annual Report on Service Performance for Market Dominant Products at 4.
[2] Library Reference USPS-FY15-29, Annual Report on Service Performance for Market Dominant Products at 4.
[3] Library Reference USPS-FY16-29, Annual Report on Service Performance for Market Dominant Products at 4.

Table II-2
International First-Class Mail Annual Targets and Percent On-Time
FY 2014 through FY 2016

First-Class Mail	Annual FY 2014[1]		Annual FY 2015[2]		Annual FY 2016[3]	
	Target (%)	On-Time (%)	Target (%)	On-Time (%)	Target (%)	On-Time (%)
Outbound Single-Piece First-Class Mail International						
Overnight		93.0		90.4		N/A
Two-Day		93.2		92.5		90.6
Three-To-Five-Day		85.7		82.5		84.5
Combined	94.0	87.8	94.0	85.3	94.0	86.2
Inbound Single-Piece First-Class Mail International						
Overnight		91.8		88.6		N/A
Two-Day		89.4		83.7		88.1
Three-To-Five-Day		82.9		71.3		77.7
Combined	94.0	85.2	94.0	75.6	94.0	81.4
Exceeded Target by:	≥0%					
Missed Target by:	>0-5%	5-10%	10-15%	15-20%	>20%	

[1] Library Reference USPS-FY14-29, Annual Report on Service Performance for Market Dominant Products at 4.
[2] Library Reference USPS-FY15-29, Annual Report on Service Performance for Market Dominant Products at 4.
[3] Library Reference USPS-FY16-29, Annual Report on Service Performance for Market Dominant Products at 4.

In the FY 2013 ACD, the Commission stated that "[t]he Postal Service must improve performance for products that did not meet the annual targets. The Postal Service should take appropriate action to improve performance for these products." FY 2013 ACD at 107.

In the FY 2014 ACD, the Commission stated that it generally "expects First-Class Mail service performance to improve in FY 2015." FY 2014 ACD at 104. For Flats, the Commission directed "the Postal Service to improve service for First-Class Mail Flats in FY 2015 or to provide an explanation in the FY 2015 ACR for why efforts to improve service performance results for First-Class Mail Flats have been ineffective and detail what changes it plans to make to improve service performance." *Id.*

In the FY 2015 ACD, among other recommendations, the Commission again directed the Postal Service "to improve service for First-Class Mail Single-Piece Letters/Postcards in FY 2016." FY 2015 ACD at 138. The Commission further required the Postal Service to "provide an explanation in the FY 2016 ACR detailing specific efforts targeted to improve service performance results for First-Class Mail Single-Piece Letters/Postcards in FY 2016." *Id.* The Postal Service was also required to "provide a detailed, comprehensive plan to improve service performance for First-Class Mail Single-Piece Letters/Postcards within 90 days of issuance of this ACD." *Id.* Finally, the Commission devoted Chapter 6 of the FY 2015 ACD to addressing performance issues with flats across all classes. *Id.* at 160-182.

The Public Representative commends the Commission for providing increased visibility and oversight into First-Class Mail service performance issues. Considering that First-Class Mail service performance is still below target levels, the Commission should continue, and possibly increase, its oversight efforts.

Regardless, the Public Representative finds it disappointing that the Postal Service has provided sparse detail of its efforts to improve service performance in its FY 2016 ACR filings. Because the Postal Service's filings lack detail, and really say nothing new compared with previous years, it gives the appearance that service performance issues are not being taken seriously. To change this appearance, the Commission should require the Postal Service to include comprehensive service performance improvement plans in future ACRs.[4] This may allow the Commission to better evaluate the Postal Service's efforts to improve service performance.

C. Standard Mail

In FY 2016, High Density and Saturation Letters, and Parcels, within Standard Mail exceeded their service performance targets. High Density and Saturation Flats/Parcels, Carrier Route, Letters, and Flats were not in compliance with meeting service performance targets. Standard Mail Flats was delivered within its service

[4] The Public Representative recognizes that the Commission followed up on performance issues after the conclusion of the FY 2015 ACD. The Public Representative would prefer that the Postal Service (without incentive from the Commission) take the initiative in improving service performance, and fully describe what actions it is taking in its ACR filings.

standard 81.4 percent of the time; an improvement of 7.6 percent over the previous year. The Standard Mail targets and on-time percentages for FY 2014 through FY 2016 are compared in Table II-3.

Table II-3
Standard Mail Annual Targets and Percent On-Time
FY 2014 through FY 2016

Standard Mail	Annual FY 2014[1]		Annual FY 2015[2]		Annual FY 2016[3]	
	Target (%)	On-Time (%)	Target (%)	On-Time (%)	Target (%)	On-Time (%)
High Density and Saturation Letters	91.0	92.3	91.0	91.5	91.0	94.9
High Density and Saturation Flats/Parcels	91.0	87.2	91.0	87.0	91.0	90.0
Carrier Route	91.0	81.4	91.0	82.0	91.0	83.9
Letters	91.0	87.1	91.0	85.8	91.0	90.1
Flats	91.0	76.2	91.0	73.8	91.0	81.4
Every Door Direct Mail - Retail	-	-	91.0	78.5	91.0	75.2
Parcels	91.0	Data Not Available	91.0	98.1	91.0	98.3
Exceeded Target by:	≥0%					
Missed Target by:	>0-5%	5-10%	10-15%	15-20%	>20%	

[1] Library Reference USPS-FY14-29, Annual Report on Service Performance for Market Dominant Products at 11.
[2] Library Reference USPS-FY15-29, Annual Report on Service Performance for Market Dominant Products at 11.
[3] Library Reference USPS-FY16-29, Annual Report on Service Performance for Market Dominant Products at 12.

In the FY 2014 ACD, the Commission directed "the Postal Service to improve service for [the Standard Mail Carrier Route and Flats] products in FY 2015 or to explain in the FY 2015 ACR why efforts to improve results have been ineffective and what changes it plans to make to improve service performance." FY 2014 ACD at 109.

In the FY 2015 ACD, the Commission stated that it "is concerned with the recent slippage in the service performance of Standard Mail Letters." FY 2015 ACD at 141. Noting that service has improved since April 2015, the Commission stated that it "expects this positive improvement in service performance to continue in FY 2016." *Id.* The Commission also expressed concern that the service performance of Every Door Direct Mail—Retail and Standard Mail High Density and Saturation Flats/Parcels were below their intended annual performance targets, and stated that it “expects service performance to improve in FY 2016.” *Id.* Finally, the Commission separately addressed the deficiencies with Standard Mail Carrier Route and Standard Mail Flats in Chapter 6 of the FY 2015 ACD. *Id.* at 142.

Although Standard Mail service appears to have generally improved, most service performance indicators are still below the applicable targets. The Commission’s oversight efforts should continue, and possibly be increased.

D. Periodicals

Neither In-County Periodicals nor Outside County Periodicals met service performance targets over the past 3 years. After a decline in service in FY 2015, the level of service provided in FY 2016 has approached the level of service previously provided in FY 2014. The Periodicals targets and on-time percentages for FY 2014 through FY 2016 are compared in Table II-4.

Table II-4
Periodicals Annual Targets and Percent On-Time
FY 2014 through FY 2016

Periodicals	**Annual FY 2014[1]**		**Annual FY 2015[2]**		**Annual FY 2016[3]**	
	Target (%)	**On-Time (%)**	**Target (%)**	**On-Time (%)**	**Target (%)**	**On-Time (%)**
In-County	91.0	80.9	91.0	77.7	91.0	80.1
Outside County	91.0	80.8	91.0	77.6	91.0	79.7
Exceeded Target by:	≥0%					
Missed Target by:	>0-5%	5-10%	10-15%	15-20%	>20%	

[1] Library Reference USPS-FY14-29, Annual Report on Service Performance for Market Dominant Products at 15.
[2] Library Reference USPS-FY15-29, Annual Report on Service Performance for Market Dominant Products at 15.
[3] Library Reference USPS-FY16-29, Annual Report on Service Performance for Market Dominant Products at 18.

In the FY 2014 ACD, the Commission directed “the Postal Service to improve service for Periodicals in FY 2015 or to explain in its FY 2015 ACR why efforts to improve results have been ineffective and what changes it plans to make to improve performance.” FY 2014 ACD at 111-112.

In the FY 2015 ACD, the Commission noted that this “was the fourth consecutive year that Periodicals did not meet its service performance target” and provided specific directives in Chapter 6 of the ACD. FY 2015 ACD at 143.

In FY 2016, the Postal Service stated that it “worked with industry to provide training to update newspapers and printers on mail preparation requirements” and continued “to use the WIP cycle time locally to identify locations and operations where the time between arrival and bundle-to-piece distribution is outside of control and working to standardize the operations involved.” Library Reference USPS-FY16-29 at 20-21.

Periodicals service performance scores have stabilized in FY 2016, but are still missing performance targets by greater than 10 percent. The Public Representative suggests that the Commission continue its oversight and visibility of the Postal Service’s efforts to improve service performance for the Periodicals products that are not meeting service performance goals.

E. Package Services

The Postal Service reported that Bound Printed Matter Parcels and Media Mail/Library Mail exceeded their service performance targets for FY 2016. However, it also reported that Bound Printed Matter Flats only met its service standard 53.6 percent of the time for FY 2015 (noting that this was an improvement from FY 2015). The Package Services targets and on-time percentages for FY 2014 through FY 2016 are compared in Table II-5.

Table II-5
Package Services Annual Targets and Percent On-Time
FY 2014 through FY 2016

Package Services	Annual FY 2014[1]		Annual FY 2015[2]		Annual FY 2016[3]	
	Target (%)	On-Time (%)	Target (%)	On-Time (%)	Target (%)	On-Time (%)
Bound Printed Matter Flats	90.0	60.2	90.0	45.2	90.0	53.6
Bound Printed Matter Parcels	90.0	99.3	90.0	99.4	90.0	99.2
Media Mail/Library Mail	90.0	91.7	90.0	91.2	90.0	92.2
Exceeded Target by:	≥0%					
Missed Target by:	>0-5%	5-10%	10-15%	15-20%	>20%	

[1] Library Reference USPS-FY14-29, Annual Report on Service Performance for Market Dominant Products at 20.
[2] Library Reference USPS-FY15-29, Annual Report on Service Performance for Market Dominant Products at 18.
[3] Library Reference USPS-FY16-29, Annual Report on Service Performance for Market Dominant Products at 22.

In the FY 2013 ACD, the Commission observed that Bound Printed Matter Flats service performance results remain the lowest among Package Services products. The Commission stated that “the Postal Service should develop strategies to enhance Full-Service mailer participation and increase service performance results.” FY 2013 ACD at 115.

In the FY 2014 ACD, the Commission again noted the decrease in service performance for Bound Printed Matter Flats.

> The Commission views the Postal Service’s previous strategies to increase performance results as largely ineffective. It directs the Postal Service to improve performance for BPM Flats in FY 2015 or include a discussion of its FY 2015 strategies to increase results and measureable volume in its FY 2015 ACR.

FY 2014 ACD at 114.

In the FY 2015 ACD, the Commission noted that the service performance of Bound Printed Matter Flats was substantially below other Package Services products for the fourth consecutive year, and provided specific directive in Chapter 6. FY 2015 ACD at 144.

In FY 2016, the Postal Service explains that:

> The mail characteristics of this product are not generally compatible with flat or package sorting equipment. As a result, these pieces are largely processed manually, often requiring additional handlings and not being presented to delivery at the finest depth of sort. Also, under current regulations, non-automated and automated BPM flats can be comingled which results in machineable pieces potentially being handled manually.
>
> The Postal Service plans to continue focusing on the improvement of Bound Printed Matter Flat processing by reducing the WIP cycle time for machine compatible pieces, thereby decreasing the time between bundle and single piece processing. This will be done by advancing the processing of Bound Printed Matter Flats to day zero (day of acceptance). The Postal Service continues to review the entry and make-up requirements for this product to improve its ability to be processed efficiently.

Library Reference USPS-FY16-29 at 24-25.

This is similar to what the Postal Service stated in FY 2015 ACR.

> …plans to focus on the improvement of Bound Printed Matter Flat processing by reducing the WIP cycle time for machine compatible pieces by decreasing the time between bundle and next handling processing. This will be done by advancing the processing of Standard Flats to day zero (day of acceptance). The Postal Service is reviewing the entry and make-up requirements for this product to improve its ability to be processed efficiently.

Library Reference USPS-FY15-29 at 21.

The Bound Printed Matter Flats service performance score, while improved from the previous year, is far from its target. The Public Representative concludes that the Postal Service's effort into improving flats service is not showing significant results. It may be time for the Commission to recommend a new approach to addressing this problem. Otherwise, there should be no expectation that service performance will improve in FY 2017.

As stated in the FY 2015 Public Representative Comments, the Commission could inquire whether or not the Postal Service believes the Bound Printed Matter Flats service performance standard (and target) is realistic.[5] If unrealistic, the Postal Service should be required to revise the service performance standard (and target). Realistic service performance standards (and targets) better inform customers of the actual service that is being provided, and allow customers to plan accordingly. A price adjustment also may be necessary so that the product's price reflects the value of service actually being provided. *See* FY 2015 Public Representative Comments at 17.

F. Special Services

The Postal Service reports that "[a]ll Special Services achieved the established service targets at the reporting level required in this report except for Post Office Box Service, which was only slightly below its target with an on-time score of 89.7 percent against the target of 90.0." Library Reference USPS-FY16-29 at 29. Other than expressing an expectation for the Postal Service to improve Post Office Box Service, the Commission did not order any actions to improve Special Services performance in the FY 2015 ACD. *See* FY 2015 ACD at 145.

Special Services targets and on-time percentages for FY 2014 through FY 2016 are compared in Table II-6.[6]

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[5] Docket No. ACR2015, Public Representative Comments, February 2, 2016 at 17 (FY 2015 Public Representative Comments).

[6] The Postal Service lists additional Special Services that are exempt from reporting at this time in Library Reference USPS-FY16-29 at 28-29.

Table II-6
Special Services Annual Targets and Percent On-Time
FY 2014 through FY 2016

Special Services	Annual FY 2014[1]		Annual FY 2015[2]		Annual FY 2016[3]	
	Target (%)	On-Time (%)	Target (%)	On-Time (%)	Target (%)	On-Time (%)
Ancillary Services	90.0	92.3	90.0	92.1	90.0	91.7
International Ancillary Services	90.0	99.7	90.0	99.7	90.0	99.7
Address List Services	90.0	33.3	90.0	100.0	90.0	N/A
Caller Services	-	E.F.R.	-	E.F.R.	-	E.F.R.
Change-of-Address Credit Card Authentication	-	E.F.R.	-	E.F.R.	-	E.F.R.
International Reply Coupon Service	-	E.F.R.	-	E.F.R.	-	E.F.R.
International Business Reply Mail Service	-	E.F.R.	-	E.F.R.	-	E.F.R.
Money Orders	90.0	98.3	90.0	99.3	90.0	99.2
Post Office Box Service	90.0	90.2	90.0	89.7	90.0	89.7
Customized Postage	-	E.F.R.	-	E.F.R.	-	E.F.R.
Stamp Fulfillment Services	90.0	98.4	90.0	97.1	90.0	99.4
E.F.R. = Exception From Reporting						
Exceeded Target by:	≥0%					
Missed Target by:	>0-5%	5-10%	10-15%	15-20%	>20%	

[1] Library Reference USPS-FY14-29, Annual Report on Service Performance for Market Dominant Products at 25.
[2] Library Reference USPS-FY15-29, Annual Report on Service Performance for Market Dominant Products at 23.
[3] Library Reference USPS-FY16-29, Annual Report on Service Performance for Market Dominant Products at 27.

In FY 2016, Post Office Box Service fell slightly under the 90.0 percent target for the second year in a row. The Postal Service continues to cite to a change in mail mix as a factor in this result. *See* Library Reference USPS-FY16-29 at 29.

As the Public Representative stated in his FY 2015 comments, for customers that rely on their mail being in their post office box by the scheduled cut-off time, missing the cut-off time effectively may add a day to the time it takes to receive their mail. *See* FY 2015 Public Representative Comments at 18-19. It also must be frustrating to customers that rely on the cut-off time and travel to a post office to pick up mail, only to find that the mail has not been placed in the Post Office Box. This may force some customers to make a second trip that day to retrieve their mail. The Public

Representative suggests that even a 90 percent success rate for this service is too low. Thus, the Public Representative urges the Commission to not only require the Postal Service to develop a plan for consistently meeting this service standard, but to develop a plan that would result in providing a much higher level of service.

Also, as previously stated in the FY 2015 Public Representative Comments, the Commission should require the Postal Service to provide an explanation of how missing the Post Office Box cut-off time affects the service performance scores for each individual class of mail.

G. Suggestions for Possible Additional Commission Actions

In the FY 2015 Public Representative Comments, he suggested that reporting calendar days-to-delivery could improve visibility into service performance for market dominant products.

> The Public Representative suggests that visibility into service performance could be improved by requiring the Postal Service to report average calendar days-to-delivery for each deliverable market dominant mail product. Reporting by days-to-delivery, instead of by Postal Service business rule days, provides customers with an actual expectation of mailing durations without having to understand the Postal Service's business rules. It also more readily captures the effects of Postal Service network changes on service expectations.[7]
>
> Using First-Class Mail for example, the Postal Service's inability to meet any of its service performance targets (based on Postal Service business rule days) indicates that service performance has deteriorated and customers are not receiving the service that they are paying for. However, the Postal Service business rule days system of measurement does not provide an adequate indication of the actual extent that mail delivery has slowed over the past several years. For example, it did not capture the effect of eliminating overnight service and moving this mail volume to 2-Day or 3-5-Day service. It also did not capture the effect of moving a substantial volume of 2-Day mail to the 3-5-Day service standard.

[7] These changes include, but are not limited to, the alignment of ZIP Code pairs with individual day to delivery service standards, potential changes in Postal Service business rules, and other Postal Service operational changes.

> A single days-to-delivery score for each First-Class Mail product would show how service changes over time. Individual single days-to-delivery scores for 2-Day and 3-5-Day mail would provide customers of an estimate of the actual calendar days it takes from entry of their mail through final delivery.[8]

FY 2015 Public Representative Comments at 19-20.

The Public Representative continues to believe that this method of reporting may provide valuable insight into the actual service being provided. This suggestion could be considered in a separate rulemaking, or potentially as one of the many options being considered for the ten year review.

H. Service Performance Conclusion

Service performance has improved from the previous reporting period, but in many areas is far from meeting service performance targets. The Commission has tried gently increasing oversight over the past few ACD cycles to get the Postal Service to improve service performance. It may be necessary for the Commission to take a more active approach that continues throughout the year to ensure improved service performance in FY 2017.

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[8] Additional visibility could be provided by disaggregating by the day of the week upon which a mail piece is entered into the system. It could be further reported by time spans that include a holiday, and those that do not.

III. CUSTOMER SATISFACTION

A. Introduction

The Postal Service must report on customer satisfaction in terms of customer access to postal services (39 C.F.R. § 3055.91) and the results of customer experience surveys (39 C.F.R. § 3055.92) when fulfilling its requirements under 39 U.S.C. § 3652(a)(2)(B)(ii).

B. Customer Access to Postal Services

39 C.F.R. § 3055.91 requires the Postal Service to report annual changes in the number of post offices and collection boxes. As part of this reporting, the Postal Service also reports on its progress towards resolving the backlog of suspended post offices.

1. Customer Access to Retail Facilities

Meaningful customer access to postal facilities is a requirement for millions of Americans. Table III-1 shows the change in the number of retail accessible facilities during FY 2016.

Table III-1
Retail Facilities

Facility Type	FY 2015	FY 2016	Change
Post Offices	26,615	26,611	-4
Classified Stations & Branches	4,461	4,451	-10
Carrier Annexes	530	523	-7
Total Postal-Managed	31,606	31,585	-21
Contract Postal Units	2,504	2,458	-46
Village Post Offices	874	877	3
Community Post Offices	536	503	-33
Total Non-Postal-Managed Facilities	3,914	3,838	-76
Total Retail Facilities	35,520	35,423	-97

Data Sources: Library Reference USPS-FY16-33, file “PostOffices.FY2016”, tab ‘Post Offices’; Library Reference USPS-FY16-17 for Postal-Managed facilities, and United States Postal Service 2016 Annual Report to Congress at 28 for Non-Postal-Managed facilities.

The Postal Service asserts that it “did not close Postal Service operated retail facilities in FY 2016.” FY 2016 ACR at 79. As the Postal Service explains, the change in the number of postal retail facilities is “the result of discontinued finance numbers and similar accounting adjustments, and do not represent the closing of any physical…facilities.” FY 2016 ACR at 79*,* n.47.

As reported in the FY 2016 ACR, the number of postal-managed retail facilities declined by 21, and the overall number of retail facilities declined by 97. *See* Table III-1. The number of non-postal-managed facilities also declined (by 76 units or approximately by 2 percent). In FY 2016 there were less contract postal units and community post offices than in FY 2015, although there were slightly more (by three units) Village Post Offices. It is not, however, clear whether the observed decline in the number of non-postal-managed units was a result (fully or partially) of actual closings or just accounting adjustments.

Considering the value of such facilities, especially in rural areas (where they are intended to replace the postal-managed facilities), the Public Representative suggests the Postal Service provide a further clarification in its reply comments.

Although the Public Representative is always concerned that all communities receive adequate access to postal services, the slight reduction in facilities (if any) does not appear to be a cause for concern in FY 2016.

2. Suspensions

Last year, the Commission stated that it “expects the Postal Service to reduce the number of facilities under suspension in FY 2016. If it is unable to do so, the Postal Service shall include a detailed explanation of why it was unable to do so in the FY 2016 Annual Compliance Report.” FY 2015 ACD at 150.

In the FY 2016 ACR, the Postal Service states that it “shares the Commission’s concern with the backlog in retail facility suspensions”, but due to directing all management’s focus towards service performance improvement in FY 2016, “the backlog of suspensions was essentially deferred." FY 2016 ACR at 80. The Postal Service reported that as "of the end of FY 2016, 264 suspended facilities had undergone the retail discontinuance process to its conclusion except for publication of the announcement of the discontinuance…." *Id.* at 81. Additionally, 391 retail units were "under suspension…at earlier stages of the review or discontinuance process."[9]

Noting the minimal (if any) progress in FY 2016 towards resolving the suspensions issue, the Public Representative urges the Commission to renew its focus on this issue. One approach might be to require the Postal Service to provide the Commission with quarterly reports on the Postal Service's progress towards reducing the number of suspended facilities.

3. Number of Collection Boxes

Table III-2 shows that there were 148,267 collection boxes available at the end of FY 2016, compared with 164,009 at the end of FY 2012. This is a decline of over 15,800 boxes or almost 10 percent over a four-year period.

Table III-2
Collection Boxes FY 2012 through FY 2016

Year	Collection Boxes
FY 2012	164,099
FY 2013	159,729
FY 2014	156,349
FY 2015	153,999
FY 2016	148,267
Percent reduction from FY 2012 to FY 2016	-9.65%

Data Sources: FY 2012 through FY 2016 ACRs, Library References 33. Note: The Postal Service filed a revised version of the FY 2015 Library Reference on February 3, 2016.

[9] *Id.* For the list of the suspended retail facilities and an additional detailed information (*e.g.,* location, reason for suspension) *see* Responses to the Chairman Information Request No. 3, Question 3, January 23, 2017, Library Reference USPS-FY16-45, file "Suspended _EOY16".

The Public Representative accepts that mailing patterns are changing, and this may justify some reduction in collection boxes. However, certain communities still rely on the availability of collection boxes to easily enter mail. The Public Representative suggests that the Commission consider a study to determine whether those communities that most heavily rely upon entering mail using collection boxes are currently receiving adequate service. This is especially relevant considering that the number of collection boxes in FY 2016 declined at a higher rate than in the previous years (by 3.7 percent in FY 2016 compared to 1.5 percent in FY 2015).

Also, as stated last year, the Public Representative believes that beyond collecting mail, collection boxes have value as a marketing tool. They serve as a visual reminder of the Postal Service. Reductions in the number of collection points may save money in the short run, but may come at the cost of reducing the Postal Service's brand awareness.

C. Wait-Time-in-Line

The FY 2016 national average for wait-time-in-line has increased by 12 seconds compared to the previous year. *See* Table III-3.

Table III-3
Average Wait-Time-In-Line
FY 2012 through FY 2016

Area	Average Wait-Time-in-Line (Minutes : Seconds)				
	FY 2012	FY 2013	FY 2014	FY 2015	FY 2016
Capital Metro	2:22	2:19	2:03	2:16	2:20
Eastern	2:24	2:16	2:00	2:04	2:12
Great Lakes	1:57	2:00	2:00	2:03	2:10
Northeast	2:23	2:21	2:28	2:38	2:40
Pacific	3:25	3:19	3:07	3:11	3:26
Southern	2:33	2:22	2:23	2:49	3:06
Western	2:58	2:48	2:47	3:06	3:25
National	2:34	2:29	2:24	2:36	2:48

Data Source: FY 2012 through FY 2016 ACRs, Library References 33.

In FY 2016, average wait-time-in-line has slightly increased in each area and for the nation as a whole. The overall wait-time-in-line still appears reasonable, and the year-to-year changes do not appear significant given the high level of aggregation at which the data are presented. However, the Public Representative remains concerned with the apparent up-tick in wait-time-in-line and suggests that the Commission continue to closely monitor this parameter of customer satisfaction.

Also, as stated last year, the Public Representative suggests that additional insight might be provided by capturing peak wait-times-in-lines, disaggregated by facility size, time of the day, month of the year, etc. This may provide a more accurate picture of the service experienced by customers.

D. Results of Customer Experience Surveys

The Postal Service measures customer satisfaction using the Customer Insights Measurement System. Table III-4 shows the change in customer satisfaction from FY 2015 to FY 2016, by customer segment. The table was developed by summing the very and mostly satisfied responses as a share of total responses for each market dominant product.

Table III-4
Customer Satisfaction with Market Dominant Products
FY 2015 through FY 2016

Market Dominant Products	Residential			Small Business			Large Business		
	FY 2015 (%)	FY 2016 (%)	Delta (%)*	FY 2015 (%)	FY 2016 (%)	Delta (%)*	FY 2015 (%)	FY 2016 (%)	Delta (%)*
	A	B	C=B-A	D	E	F=E-D	G	H	I=H-G
First-Class Mail	89.22	89.13	-0.09	84.77	83.34	-1.43	83.27	81.49	-1.78
Single-Piece International Mail	85.80	84.80	-1.00	82.31	81.34	-0.97	82.65	74.37	-8.28
Standard Mail	85.11	85.49	0.38	80.82	79.87	-0.95	79.49	76.89	-2.60
Periodicals	85.50	85.06	-0.44	82.42	81.85	-0.57	77.10	74.26	-2.84
Single-Piece Standard Post	86.66	86.28	-0.38	82.65	81.12	-1.53	77.81	75.85	-1.96
Bound Printed Matter	n/a	n/a	n/a	81.70	80.11	-1.59	76.54	73.40	-3.14
Media Mail	87.17	86.59	-0.58	85.18	84.06	-1.12	78.61	74.28	-4.33
Library Mail	85.10	85.54	0.44	85.43	83.05	-2.38	78.66	70.56	-8.10
Color coding:	Mail classes with lower customer satisfaction scores in FY 2016 than in FY 2015.								

* refers to percentage point change
n/a = data not available
Data Sources: Library Reference USPS-LR-FY16-38; FY 2015 ACR, Library Reference USPS-LR-FY15-38.

In general, customer satisfaction has declined for nearly every market dominant product. The greatest declines were observed for large business customers, followed by small business customers, and to a lesser extent by residential customers. Even though the Postal Service appears to be improving service performance, this improvement does not carry over to an increase in customer satisfaction. As stated in his FY 2015 comments, the Public Representative again suggests that the Commission closely monitor customer satisfaction to ensure that further declines do not occur.

IV. MARKET DOMINANT PRODUCTS

A. Introduction

In the FY 2016 ACR, the Postal Service notes that pursuant to Commission Order No. 3506, "the calculation of attributable costs will be changing".[10] FY 2016 ACR at 4. The attributable costs of a market dominant product will include not only its volume variable and product specific costs (as in prior years), but also "the product's inframarginal costs developed as part of the estimation of the product's incremental costs." FY 2016 ACR at 4. The Postal Service discusses several obstacles that do not allow calculating the product's inframarginal costs. *Id.* at 4-5. In the FY 2016 CRA report, the Postal Service revises the title of the column previously labeled "Attributable" [costs] to "Volume Variable & Product Specific" [costs], but indicates that this revision is "cosmetic", and is not a reflection of any changes in costing methodology requested by Order No. 3506. FY 2016 ACR at 7. In light of Commission Orders Nos. 3506 and 3641, and because the Postal Service does not estimate inframarginal costs for market dominant products, the Public Representative considers the sum of volume variable and product specific costs to be a *proxy* of attributable costs. In other words, the Public Representative concludes that when the Postal Service states that a product fully covers its "costs," it means that it covers only a "proxy" of attributable costs.

Most market dominant products covered attributable costs in FY 2016. A class-by-class analysis follows. The market dominant products that did not cover attributable costs are shown in Table IV-1. Total losses for these market dominant products and

[10] *See* Docket No. RM2016-2, Order Concerning United Parcel Service, Inc.'s Proposed Changes to Postal Service Costing Methodologies (UPS Proposals One, Two, and Three), September 9, 2016, (Revised October 19, 2016) at 60 (Order No. 3605). *See also*, Docket No. RM2016-13, Order Adopting Final Rules on Changes Concerning Attributable Costing, December 1, 2016 (Order No. 3641).

services (excluding negotiated service agreements) were approximately $1,390 million (an increase of greater than 11 percent from FY 2015).[11]

Table IV-1
FY 2016 Financial Results for Market Dominant Products and Services with Cost Coverage Below 100 percent

Product/Services	Cost Coverage (%)	Loss ($ Millions)	Unit Loss (cents)
First-Class			
Inbound Letter Post	67.6	128.0	32.6
Periodicals			
Within County	70.1	26.0	4.9
Outside County	73.7	512.4	10.1
Standard Mail			
Flats	79.7	601.9	9.5
Parcels	63.8	30.1	67.3
Package Services			
Media and Library Mail	75.2	88.0	117.3
Special Services			
Collect on Delivery (COD)	41.1	2.9	1,444.7
International Ancillary Services	99.2	0.4	1.26
Stamp Fulfillment Services	87.3	0.5	N/A
Total:		1,390	

Data Sources: Library Reference USPS-FY16-1, file "Public-FY16CRAReport", tabs 'Cost1' and 'Cost 2'; FY 2016 ACR (Revised on January 25, 2017) at 12.

B. First-Class Mail Cost Coverage

In FY 2016, most First-Class Mail products covered attributable costs, with the exception of International Inbound [Single-Piece] Letter Post. In FY 2016, the cost coverage for the First-Class Mail class was 224.5 percent, and unit contribution was 25.7 cents. FY 2016 ACR at 12 (Revised January 25, 2017). First-Class Mail, as a

[11] Library Reference USPS-FY16-1, file "Public-FY16CRAReport", tabs 'Cost1' and 'Cost 2'; FY 2016 ACR (Revised January 25, 2017), Library Reference USPS-FY15-1, file "Public-FY15CRA", tabs 'Cost1' and 'Cost 2'.

class, continued to provide a significant contribution to institutional costs ($15.937 billion or 72.4 percent of the overall contribution provided by market dominant mail products).[12]

In FY 2016, the cost coverage for Inbound Letter Post was 67.6 percent. FY 2016 ACR at 12 (revised January 25, 2017). This is 4.3 percentage points lower than in FY 2015 (when the product's cost coverage was 71.9 percent).[13] While in FY 2014-2015 the cost coverage for Inbound Letter Post was increasing, in FY 2016 the cost coverage decreased, and the reported loss was the highest over a seven year period. *See* Chart IV-1. The FY 2016 volume for Inbound Letter Post increased by 23.1 percent since FY 2015, which together with the decrease in cost coverage resulted in a significant increase (by greater than 30 percent) in the product's reported total loss; from $97.9 million in FY 2015 ($74.8 million in FY 2014) to $128.0 million in FY 2016.[14]

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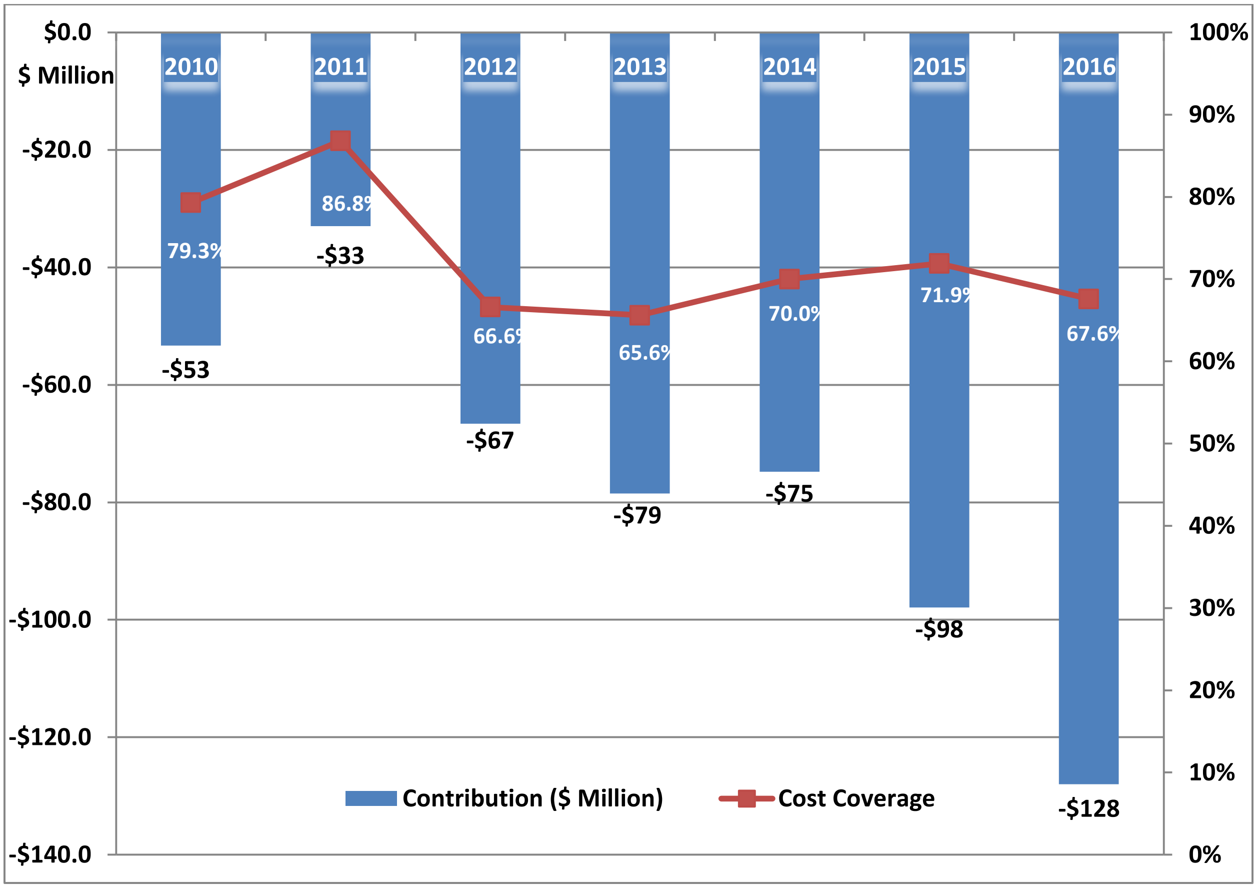
[12] *See* Library Reference USPS-FY16-1, file “Public-FY16CRAReport”, tab ‘Cost1’; FY 2016 ACR at 12 (Revised January 25, 2017).

[13] *See Id.* and FY 2015 ACR, Library Reference PRC-LR-ACR2015/1, file “15 Summary_LR1”, tab ‘FCM’.

[14] *See* Library Reference USPS-FY16-1, file “Public-FY16CRAReport”, tab ‘Cost1’ and ‘Volume1’; FY 2016 ACR at 12 (Revised January 25, 2017); FY 2015 ACR, file “15 Summary_LR1”, tab ‘FCM’; FY 2014 ACR, Library Reference PRC-LR-ACR2014/1, file “14 Summary_LR1”, tab ‘FCM’.

Chart IV-1
FY 2010 through FY 2016
Financial Results for Inbound Letter Post



Data Sources: Library Reference USPS-FY16-1 file "Public_FY16CRAReport", tab 'Cost1'; FY 2016 ACR (Revised on January 25, 2017) at 12. FY 2015 ACR, PRC-LR-ACR2015/1, file "15 Summary_LR1", tab 'FCM'; FY 2014 ACR at 53; FY 2012 ACR, PRC-LR-ACR2012/1, file "12 Summary_LR1", tab 'FCM'; FY 2011 ACR, PRC-LR-ACR2011/1, file "11 summary_lr1", tab 'FCM' and FY 2010 ACR, PRC-LR-ACR2010/1, file "10 Summary_LR1", tab 'FCM'.

In the Postal Service's FY 2016 ACR discussion of the failure of Inbound Letter Post to cover attributable costs, the Postal Service emphasized "the product's unique pricing regime," and the inability to "independently determine the prices for delivering foreign origin mail." FY 2016 ACR at 13. In the FY 2014-2015 ACDs, the Commission expressed hope that the new compensatory terminal dues formula (effective January 2014) would have a positive impact on the Inbound Letter Post revenue and cost coverage. *See* FY 2015 ACD at 70, FY 2014 ACD at 53. However, as the Postal Service explains, the formula for Inbound Letter Post from *Transition Countries* is [still] based on a flat rate per kilogram, instead of actual costs." (Emphasis added). FY 2016 ACR at 13. However, in the recently revised Library Reference USPS-FY16-NP2, the reported cost coverage for Inbound Letter Post from Target Countries is still below 100 percent.[15] In the FY 2016 ACR Notice of Errata, the Postal Service confirms that Inbound Letter Post "pieces from neither group (at UPU rates) covered costs in FY 2016".[16] The Postal Service also noted that Inbound Letter Post bilateral agreements with a number of countries "maintained a healthy coverage and provided a substantial positive contribution." FY 2016 ACR Notice of Errata at 2.

In the FY 2014 and FY 2015 ACDs, the Commission recognized "the pricing regime for the Inbound Letter Post, based upon the current UPU formula" and did not recommend any immediate remedial action. *See* FY 2015 ACD at 70, FY 2014 ACD at 53-54. The Commission, however, recommended that the Postal Service continue its efforts that would result in an improved financial position*. Id.* In the FY 2016 ACR, the Postal Service briefly describes the ongoing efforts and suggested that the increases in terminal dues for Inbound Letter Post scheduled for the next calendar year should be beneficial. FY 2016 ACR at 13-14. Given the unique pricing regime of the Inbound Letter Post, the Public Representative cannot conclude that First-Class Mail rates were out of compliance in FY 2016 within the provisions of chapter 36 of title 39.

For First-Class Parcels (which did not cover costs in FY 2012 and FY 2013), the cost coverage in FY 2014 was greater than 100 percent, and continued to increase in FY 2015 and FY 2016. *See* Chart IV-2. In FY 2016, the product's contribution to

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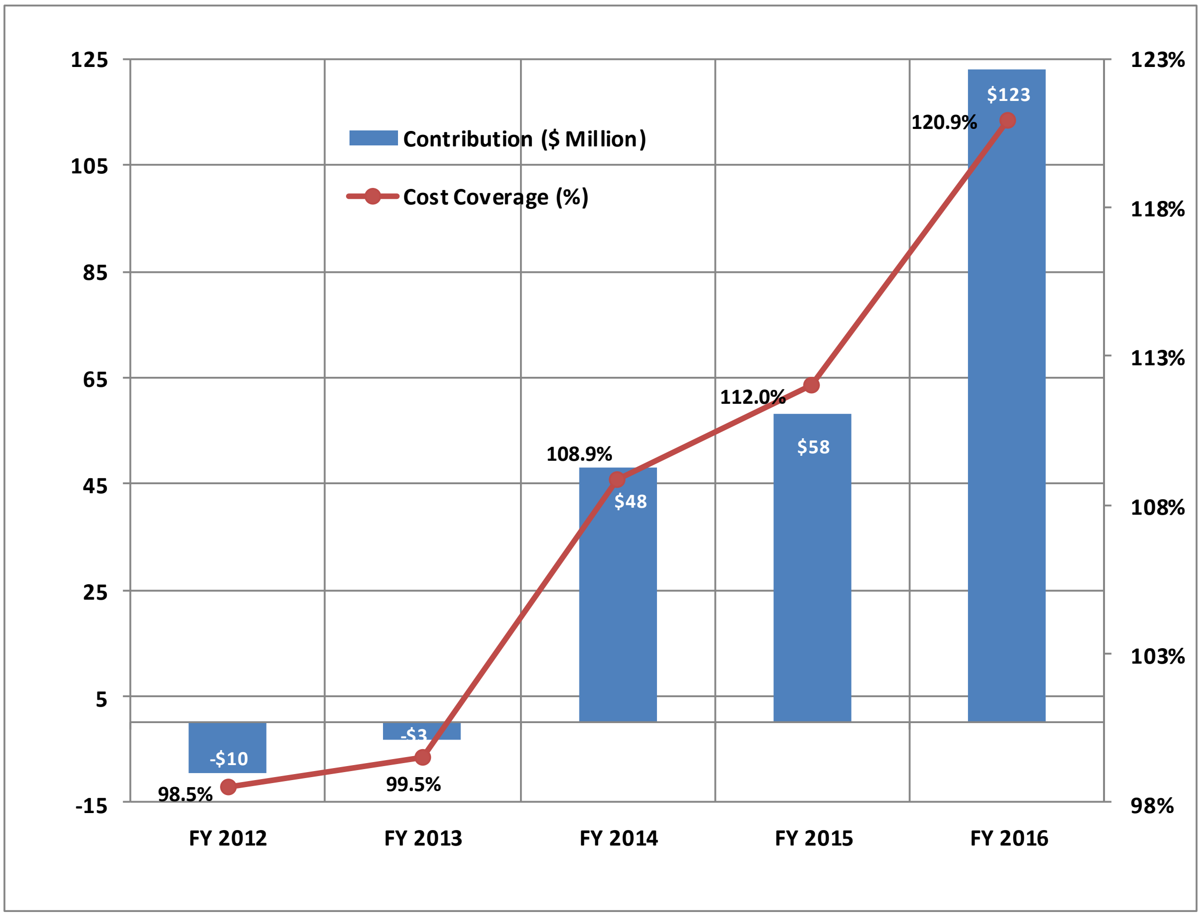
[15]*See* Library Reference USPS-FY16-NP2 (Revised January 19, 2017), file "Reports (Unified)", tab 'A Pages (md).' The library reference was provided in response to a Chairman Information Request and filed under seal. *See* Response of the United State Postal Service to Questions 1-4 of Chairman's Information Request No. 5, Question 3-4, January 19, 2017.

[16] Notice of the United States Postal Service of Filing of Revised Annual Compliance Report Pages – Errata, January 25, 2017 at 1 (FY 2015 ACR Notice of Errata).

institutional costs more than doubled (it increased from $58.4 million in FY 2015 to $123.1 million in FY 2016).[17] In FY 2016, unit contribution increased by 19.3 cents (from 29.2 cents in FY 2015 to 48.5 cents in FY 2016). *Id.*

Chart IV-2
FY 2012 through FY 2016
Financial Results for Domestic First-Class Mail Parcels



Data Sources: FY 2016 ACR at 12; FY 2015 ACR, PRC-LR-ACR2015/1, file “15 Summary_LR1”, tab ‘FCM’; FY 2014 ACR, PRC-LR-ACR2014/1, file “14 Summary_LR1”, tab ‘FCM’; FY 2013 PRC Financial Report, Revised April 10, 2014 at 43-44; FY 2012 ACD, Appendix D, Table D1.

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[17] Library Reference USPS-FY16-1, file “Public_FY16CRAReport”, tab ‘Cost1’; FY 2015 ACR, Library Reference PRC-LR-ACR2015/1, file “15 Summary_LR1”, tab ‘FCM’.

C. Standard Mail Cost Coverage

In FY 2016, the Standard Mail class continued to be the largest mail class by volume, representing more than half (54.0 percent) of all market dominant mail volume, and 29.6 percent of the total market dominant products' contribution to institutional costs.[18] In FY 2016, the cost coverage for Standard Mail was 158.3 percent, and the overall dollar contribution of Standard Mail to institutional costs was $6.51 billion (compared to $15.9 billion for First-Class Mail). FY 2016 ACR at 12, 24.

In FY 2016, Standard Mail products (except for Standard Flats and Standard Parcels) covered attributable costs. FY 2016 ACR at 24. In FY 2016, Standard Parcels and Standard Flats provided negative contribution to institutional costs, which raises a concern about compliance with Section 3622(c)(2) of title 39, as discussed below.

1. Standard Mail Parcels

The unit institutional burden of Standard Mail Parcels increased significantly (from 40.2 cents in FY 2015 to 67.3 cents in FY 2016), and cost coverage decreased from 72.8 percent to 63.8 percent during the same time period.[19] In the FY 2016 ACR, the Postal Service claims that the current failure of Standard Mail Parcels to cover costs is "due to a slight increase in labor costs combined with the substantial decrease in parcel volume," as well as to a larger share of irregular parcels (that has relatively lower cost coverage). FY 2016 ACR at 24-25. Standard Mail Parcel volume decreased by more than 25 percent (from 60.4 million pieces in FY 2015 to 44.8 million pieces in FY 2016), and the overall institutional burden increased to $24.3 million in FY 2015 to $30.1 million in FY 2016. *Id.*

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[18] *See* Library Reference USPS-FY16-1, file "Public-F16CRAReport", tabs 'Volume1' and 'Cost1'; FY 2016 ACR at 12 (Revised January 25, 2017).

[19] *See Id.* and FY 2015 ACR, Library Reference PRC-LR-FY15-1, file "15 Summary_LR1", tab 'Standard.'

In the FY 2014 and FY 2015 ACDs, the Commission found that the product's revenues were not sufficient to cover attributable costs, but concluded that that the Postal Service's approach to improve cost coverage through above-average price increases would be appropriate. FY 2014 ACD at 50, FY 2015 ACD at 66-67. In the FY 2016 ACR, the Postal Service affirms its commitment to improve the Standard Mail Parcels "product's cost coverage by proposing above-average price increases in future…price adjustments." FY 2016 ACR at 25. As the Postal Service notes in Docket No. R2017-1, the price increase for Standard Mail Parcels was 1.583 percent, or 76 percent higher than the average class level price increase.[20]

The Public Representative suggests that the Commission require the Postal Service to improve the productivity of Standard Mail Parcels in addition to continue to implement above-average price increases.

2. Standard Mail Flats

In FY 2016, the cost coverage for Standard Mail Flats decreased slightly (from 80.1 percent in FY 2015 to 79.7 percent in FY 2016 or by less than a half percentage point).[21] However, the overall contribution to the institutional burden increased significantly (from $519 million in FY 2015 to $602 million in FY 2016 or by more than 15 percent).[22] This is not surprising considering a significant (by more than 1 million

[20] *Id. See also,* Docket No. R2017-1, Order on Price Adjustments for First-Class Mail, Standard Mail, Periodicals, and Package Services Products and Related Mail Classification Changes, November 15, 2016 at 29 (Order NO. 3610).

[21] Library Reference USPS-FY16-1, file "Public-F16CRAReport", tab 'Cost1'; FY 2015 ACR, Library Reference PRC-LR-ACR2015/4, file "Chapter III, Standard Mail Tables (Flats and Parcels) 2015", tab 'SM Flats III (1)'.

[22] *Id.* The Public Representative has noticed a certain discrepancy between the FY 2015 financial results presented by the Postal Service in the FY 2016 ACR Report. Thus, it is not clear if FY 2015 cost coverage was 80.3 percent (as indicated on page 38 of the report), or 80.1 percent (which follows from the statement on page 25 that the cost coverage of 79.7 percent was down by 0.4 percentage points from FY 2015). Therefore, when referring to the FY 2015 cost coverage and institutional burden numbers, the Public Representative uses FY 2015 ACR, Library Reference PRC-LR-ACR2015/4.

pieces) increase in Standard Mail volume from 5,260 million pieces in FY 2015 to 6,307 million pieces in FY 2016.[23] As illustrated by Chart IV-3, the contribution has been steadily decreasing for Standard Mail Flats for the third consecutive year. A potential benefit of the decrease in cost per piece by 3 cents (from 50.1 cents in FY 2015 to 47.1 cents in FY 2016) was almost eliminated by a 2.7 cents decline in revenue per piece (from 40.2 cents in FY 2015 to 37.5 cents in FY 2016).[24] As a result, per piece institutional cost burden decreased slightly (from 9.9 cents in FY 2015 to 9.5 cents in FY 2016 or by approximately 0.4 cents).[25]

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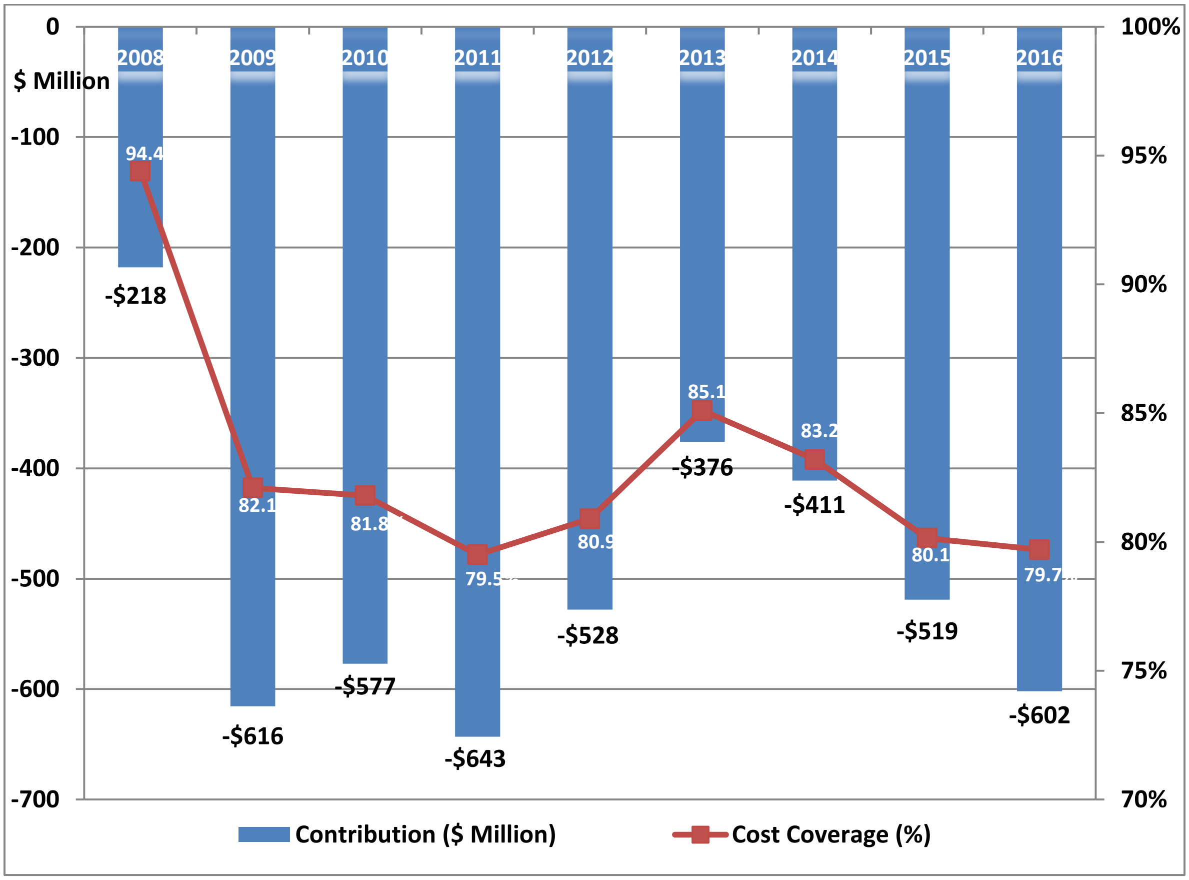
[23] Library Reference USPS-FY16-1, file "Public-F16CRAReport", tab 'Volume1'; FY 2015 ACR, Library Reference PRC-LR-FY15-1, file "15 Summary_LR1", tab 'Standard.'

[24] Library Reference USPS-FY16-1, file "Public-F16CRA', tab 'Cost1'; FY 2015 ACR, Library Reference PRC-LR-ACR2015/4, file "Chapter III, Standard Mail Tables (Flats and Parcels) 2015", tab 'SM Flats III (1).'

[25] Library Reference USPS-FY16-1, file "Public-F16CRAReport", tab 'Cost1'; FY 2015 ACR, Library Reference PRC-LR-ACR2015/4, file "Chapter III, Standard Mail Tables (Flats and Parcels) 2015", tab 'SM Flats III (2)'. However, the Postal Service warns that when comparing the reported unit costs for Standard Mail Flats in FY 2016 and FY 2016, it is necessary to consider the effects of the classification changes occurred in this period (migration of Carrier Route mail volumes to Standard Mail Flats). FY 2016 ACR at 25, 35-37.

Chart IV-3
FY 2008 through FY 2016
Financial Results for Standard Mail Flats



Data Sources: Library Reference USPS-FY16-1, file "Public-F16CRA', tab 'Cost1'; FY 2015 ACR, PRC-LR-ACR2015/4, file "Chapter III, Standard Mail Tables (Flats and Parcels) 2015", tab 'SM Flats III (1).

In the FY 2014 ACD, the Commission expressed a concern "that the product's financial performance [had] diverged from the positive trend demonstrated in the last two fiscal years". FY 2014 ACD at 48. As illustrated in Chart IV-3, the decrease in cost coverage has been observed for the third year after a few years of improvement in Standard Mail Flats cost coverage. In the FY 2015 ACD, the Commission concluded that the Postal Service was "unsuccessful in reducing costs…for flats," and "did not identify a comprehensive plan to ameliorate the [financial] problem." FY 2015 ACD at 162.

In connection with the FY 2010 ACD directives, the Postal Service reports on the operational and costing methodology changes that took place in FY 2016. FY 2016 ACR at 27-38. The Postal Service also provides "a statement summarizing the historical and current fiscal year subsidy of the flats product; and the estimated timeline for phasing out this subsidy." *Id.* at 27.

It is important to note that in the FY 2015 ACD, the Commission clearly articulated "its concerns with the Postal Service's inability to qualify the cost savings of its initiatives to reduce costs for flats". FY 2015 ACD at 64. In the FY 2016 ACR, the Postal Service states that, where possible, it "has developed key metrics to monitor and gauge the operational impact of changes, specifically related to flat mail processing." FY 2016 ACR at 27. The Public Representative acknowledges the Postal Service's efforts to improve productivity and efficiency of flats processing.[26] The Postal Service, however, still asserts that it is "unable to provide an estimate of the financial impacts of [the] operational changes at this time." FY 2016 ACR at 28. Although the Postal Service confirms that it is going to increase the price for Standard Mail "by at least CPU times 1.05 during the next general market-dominant price change," it traditionally states that "it is very difficult to predict when the shortfall for Standard Mail Flats will be phased out" maintaining that it "will not be eliminated prior to commencement of the comprehensive review of the present regulatory system." *Id.* at 37.

Based on analysis of the information presented in the FY 2016 ACR, the Public Representative cannot conclude that the Postal Service fully followed the Commission's directives regarding cost reduction for Standard Mail Flats.

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[26] *See* FY 2015 ACD, Response of the United States Postal Service to Commission Information Request No. 1, November 28, 2016.

D. Periodicals Cost Coverage

The Postal Service reports that in FY 2016, both Periodicals products (In-County and Outside County) failed to cover attributable costs, and the cost coverage for both products further declined in comparison with FY 2015. FY 2016 ACR at 51. For the Periodicals class, the cost coverage was 74.0 percent in FY 2016 (1.7 percentage points less than in FY 2015).[27] As illustrated in Chart IV-4, Periodicals have consistently failed to cover attributable costs since enactment of the PAEA in 2006. In FY 2016, unit cost for Periodicals was 36.5 cents (0.5 cent higher than in FY 2015), and unit contribution to institutional burden was 9.5 cents (0.7 cents higher than in the previous year). *Id.* The FY 2016 Periodicals volume constitutes less than two third of the FY 2007 volume (after declining from 8,795 million in FY 2007 to 5,586 million in FY 2016), with the annual rate of volume decline ranging between 2.2 and 8.6 percent. *Id. See* Chart IV-5. In FY 2016, Periodicals revenue decreased by 5.2 percent, and volumes decreased at a lower rate (by 4.3 percent). *Id.* As the Postal Service explains, the FY 2016 decrease in cost coverage was due to both the increase in unit cost and the decrease in unit revenue (by 0.74 percent and 1.4 percent, respectively). FY 2016 ACR at 52.

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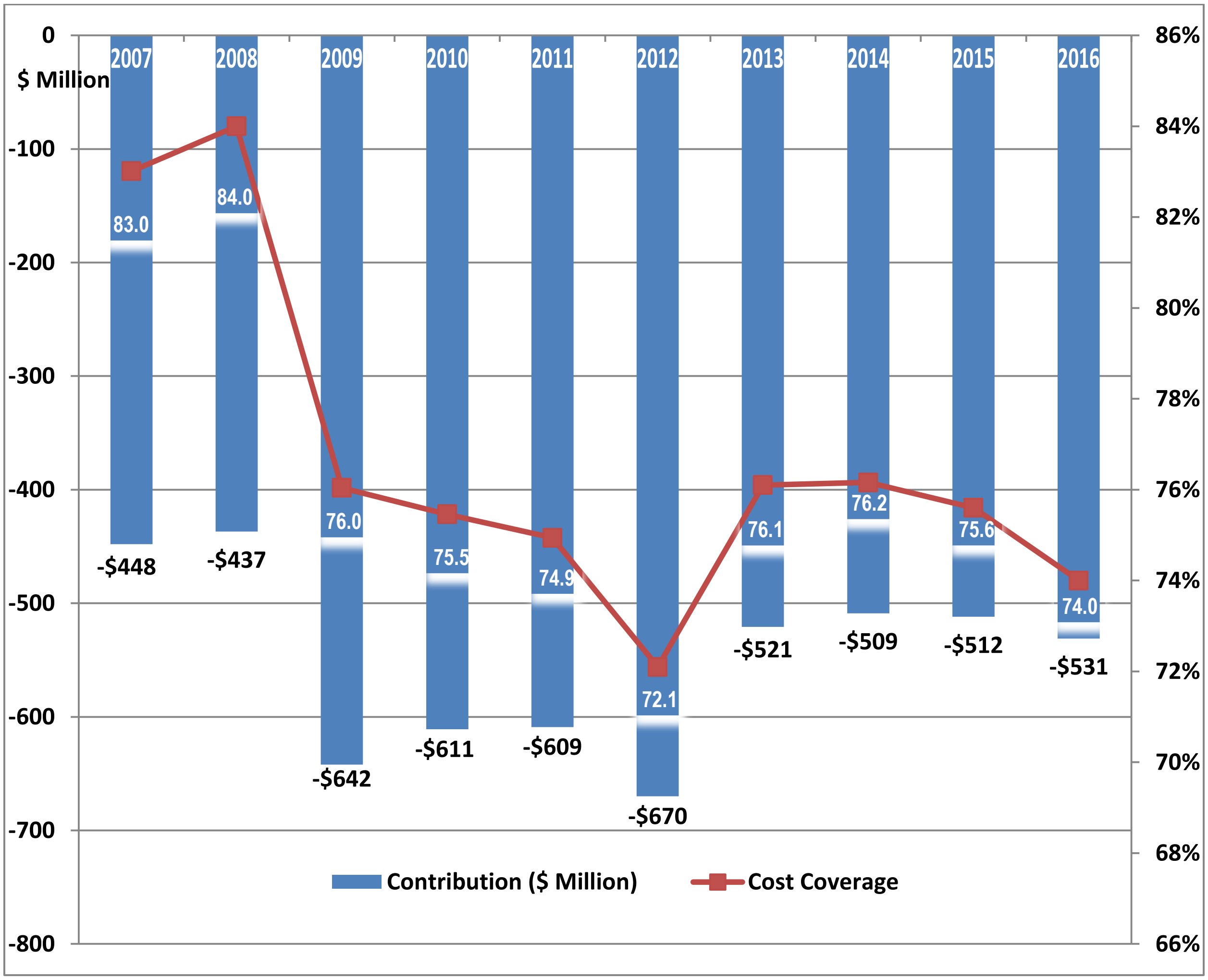
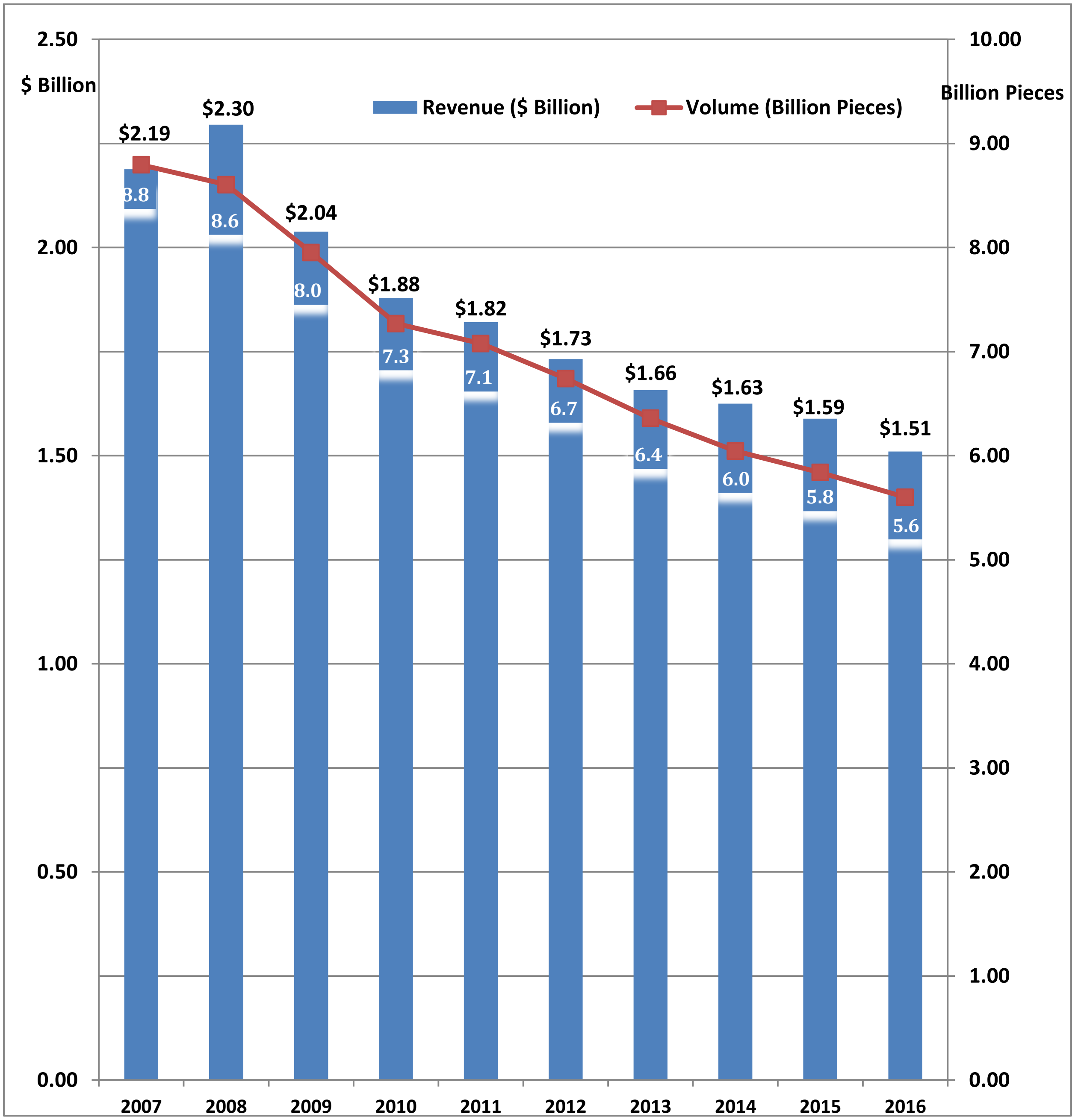
[27] *See* Library Reference USPS-FY16-1, file "Public_F16CRAReport", tab 'Cost1' and FY 2015 ACR, Library Reference PRC-LR-ACR2015/1, file "15 Summary_LR1", tab 'Periodicals.'

Chart IV-4
FY 2007 through FY 2016
Financial Results for Periodicals



Data Sources: Library Reference USPS-FY16-1, file "Public_F16CRAReport", tab 'Cost1' and FY 2015 ACR, PRC-LR-ACR2015/5, file "FY15 periodicals cost coverage", tab 'Historical Cost Coverage.'

Chart IV-5
FY 2007 through FY 2016
Volumes and Revenues for Periodicals



Data Sources: USPS-FY16-1, file “Public_F16CRAReport”, tabs ‘Cost1’, ‘‘Volume1’ and FY 2015 ACR, PRC-LR-ACR2015/5, file “FY15 periodicals cost coverage”, tab ‘Historical Cost Coverage.’

In the FY 2014 ACD, the Commission emphasized the importance of "examining the underlying reasons why the Periodicals class failed to meet the Postal Service's financial projections," including those reflected in Docket No. R2013-11. FY 2014 ACD at 35. In the FY 2015 ACD, the Commission found that the Postal Service "failed to meaningfully address the FY 2014 ACD directive" to present a report addressing the pricing issues including but not limited to the "progress in improving pricing efficiency." FY 2015 ACD at 23-24. The Commission further directed the Postal Service to submit the report within 120 days of the issuance of that ACD and include the updated version of the report with the FY 2016 ACR. *Id.* at 24.

Following the Commission's directives, the Postal Service filed the report on July 26, 2016, and provided the updated version of the report with the FY 2016 ACR.[28] Explaining why postage rates for the Periodicals class have been traditionally kept relatively low, the Postal Service emphasizes the "intrinsic societal value" of the class.[29] The Postal Service also argues that the price cap imposed by Section 3622(d) of Title 39, "significantly limits the…ability to increase the cost coverage for Periodicals products through price increases."[30] Moreover, the Postal Service maintains that due to the existence of different factors that could affect Periodicals revenue (*i.e.,* changes to mail preparation rules), it is not possible to "explicitly measure the impacts of the…price change on revenue, cost or contribution."[31]

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[28] *See* FY 2015 ACR, Third Response of the United States Postal Service to Commission Requests for Additional Information in the FY 2015 Annual Compliance Determination, July 26, 2016 at 1-13 (Periodicals Report); FY 2016 ACR, Library Reference USPS-FY16-44, Update to Periodicals Pricing Report (Update to Report).

[29] Periodicals Report at 1; Update to Report at 1-2.

[30] Periodicals Report at 2; Update to Report at 2.

[31] Update to Report at 2, 7.

Despite the Commission's consistent requests for the Postal Service to quantify the financial impact of Periodicals operations in earlier ACDs, the Postal Service did not provided a material response to these inquiries in its FY 2015 ACR.[32]

E. Package Services Cost Coverage

In FY 2016, cost coverage for Package Services was 102.3 percent. FY 2016 ACR at 54. This is 2.6 percentage points less than the FY 2015 costs coverage of 104.9 percent, and 10.2 percentage points less than the FY 2014 cost coverage of 112.5 percent.[33] Although in FY 2016, the cost coverage for Package Services continued to decrease, the class has produced sufficient revenues to cover attributable costs (after being underwater in FY 2012 when the cost coverage was 97.7 percent).[34] In FY 2016, the cost per piece was $1.32 (3 cents lower than the $1.36 cost per piece observed in FY 2015), and the revenue per piece was $1.35 (approximately 7.5 cents lower than the FY 2015 revenue per piece of $1.43).[35]

The Postal Service claims that the decrease in the cost coverage for the overall class is largely due to a significant decline in the cost coverage for Bound Printed Matter (BPM) Parcels (118.7 percent to 104.3 percent, or by more than 14 percentage points). FY 2016 ACR at 55. Media Mail/Library Mail traditionally does not cover attributable costs. Its cost coverage declined by approximately 1 percentage point (from 76.2 percent in FY 2015 to 75.2 percent in FY 2016).[36] Negative unit contribution increased slightly (from $1.14 per piece to $1.17 per piece), and the overall institutional burden

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[32] FY 2014 ACD at 40-41; FY 2015 ACD at 160-163.

[33] *See* Library Reference USPS-FY16-1, file "Public_F16CRAReport", tab 'Cost1'; FY 2015 ACR, Library Reference PRC-LR-ACR2015/1, file "15 Summary_LR1", tab 'Package Services' and FY 2014 ACR, Library Reference PRC-LR-ACR2014/1, file "14 Summary_LR1", tab 'Package Services.'

[34] *See* FY 2012 ACD at 128.

[35] *See* Library Reference USPS-FY16-1, file "Public_F16CRAReport", tab 'Cost1'; FY 2015 ACR, Library Reference PRC-LR-ACR2015/1, file "15 Summary_LR1", tab 'Package Services.'

[36] *Id.* Media Mail/Library Mail has not covered its attributable costs for the tenth consequent year. *See* FY 2015 ACD at 67; FY 2014 ACD at 50; FY 2013 ACD at 57.

accounted for $88.0 million in FY 2016 (which is $2.6 million or 3 percent more than in FY 2015).[37]

In the FY 2015 ACD, the Commission stated that Media Mail/Library Mail did not cover attributable costs, which made the product's financial results inconsistent with the requirements of 39 U.S.C. § 3622(c)(2). FY 2015 ACD at 67. However, the Commission emphasized the value of Media Mail/Library Mail as outlined in 39 U.S.C. § 3622(c)(11), and supported "the Postal Service's approach to improve cost coverage through above-average price increases." *Id.* at 67-68. In the FY 2016 ACR, the Postal Service confirmed its commitment to continue with above average price increases. FY 2016 ACR at 55. The Postal Service also followed the Commission's encouragements "to explore opportunities to further reduce the unit cost of Media Mail/Library Mail." FY 2015 ACD at 68. In FY 2016, the unit cost declined by 7 cents (although unit revenue declined at a higher pace—by more than 10 cents). FY 2016 ACR at 55.

Considering the value of Media Mail/Library Mail, certain improvements in the product's unit costs, as well as the Postal Service's intention to continue with above average price increases, the Public Representative does not recommend any specific remedies at this time. However, the Public Representative has a concern regarding the rapid decrease in cost coverage for BPM Parcels in FY 2016, which if it continues could cause the whole Package Services class to be "under water." The Public Representative suggests that the Postal Service perform a comprehensive analysis of the factors that lead to an increase in unit cost and/or increase in unit revenue for BPM Parcels, and attempt to minimize their impact in the near future.

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[37] *See* Library Reference USPS-FY16-1, file "Public_F16CRAReport", tab 'Cost1'; FY 2015 ACR, Library Reference PRC-LR-ACR2015/1, file "15 Summary_LR1", tab 'Package Services.'

F. Special Services Cost Coverage

As reported in the FY 2016 CRA (summarized in Table IV-I above), three special services failed to cover their costs in FY 2016: Collect on Delivery (COD), International Ancillary Services, and Stamp Fulfillment Services. *See* Table IV-2. This is an increase over the previous three years when only one type of service, Stamp Fulfillment Services, did not cover costs.

Table IV-2
FY 2013 through FY 2016
Cost Coverage for Market Dominant Special Services with Cost Coverage Below 100 percent in FY 2016

Special Services	**In Percentage (%)**			
	FY 2016	**FY 2015**	**FY 2014**	**FY 2013**
Domestic Special Services				
Cost of Delivery (COD)	41.1	103.0	134.6	119.7
Stamp Fulfillment Services (SFS)	87.3	85.1	82.3	80.8
International Special Services				
International Ancillary Services	99.2	316.9	321.7	196.4

Data Sources: Library Reference USPS-FY16-1, file “Public_F16CRAReport”, tab ‘Cost2’; FY 2015 ACR (Revised) at 52; Library Reference USPS-FY15-1, file “Public-FY15CRA”, tab ‘Cost2’; FY 2014 ACR, file “public_fy14cra”, tab ‘Cost2’; Library Reference USPS-FY13-1, file “F13PublicCRA”, tab “Cost2”; FY 2015 ACR, Library Reference PRC-LR-ACR2015/7, file “prc-lr-acr2015-7 fy 2015 special services”, tab ‘Unit Rev & Cost & CC’.[38]

1. Collect on Delivery (COD)

In FY 2016, the revenue generated by COD covered slightly more than 40 percent of the COD costs. *See* Table IV-2. The Postal Service explains that in FY 2016, the number of COD transactions significantly decreased, which resulted in a limited number of “observations during sampling process.” FY 2016 ACR at 62. The Postal Service indicates that the above average price increase proposed in Docket No.

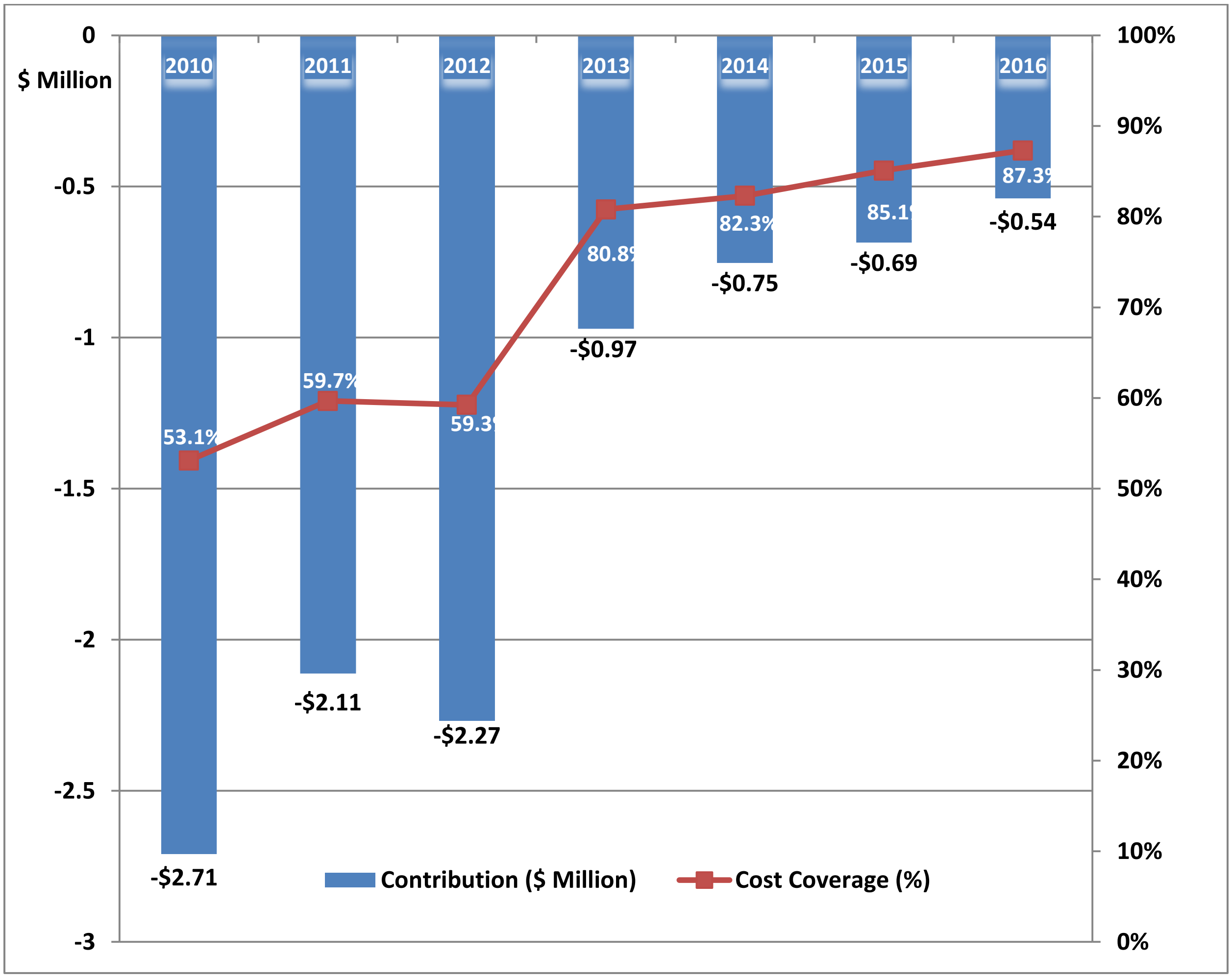
[38] For consistency reasons, for all services (with the exception of SFS), the Public Representative refers to the applicable ACR numbers reported in the CRA. The revenue provided in other data sources usually includes fees and is generally higher than the CRA revenue (which also results in higher cost coverage).

R2017-1, combined with the "different sampling results" should lead to the cost coverage exceeding 100 percent. *Id.* However, the Postal Service does not describe why it anticipates "different sampling results" and whether it is going to modify the sampling process (*e.g.,* by changing sampling method, including a higher number of observations into sample). The Public Representative suggests that the Postal Service provide some additional information to clarify this issue.

2. Stamp Fulfillment Services

The Postal Service emphasizes that although cost coverage for Stamp Fulfillment Service was below 100 percent in FY 2016, it was still "the highest cost coverage for SFS ever." FY 2016 ACR at 63. In the FY 2015 ACD, the Commission performed a comprehensive analysis of Stamp Fulfillment Service's six-year financial performance, and stated that cost coverage for Stamp Fulfillment Service "improved substantially since FY 2012, showing increases each year." FY 2015 ACD at 68. As illustrated by Chart IV-6, Stamp Fulfillment Service financial results continue to improve. Considering the steady improvement of Stamp Fulfillment Service financial performance, the Public Representative concludes that the Postal Service is on the right track to Stamp Fulfillment Service covering its costs.

Chart IV-6
FY 2010 through FY 2016
Financial Results for Stamp Fulfillment Services



Data Sources: Library Reference USPS-FY16-1, file "Public_F16CRAReport", tab 'Cost2'; FY 2015 ACR, Library Reference PRC-LR-ACR2015/7, file "prc-lr-acr2015-7 fy 2015 special services", tab 'Unit Rev & Cost & CC'.

3. International Special Services

In FY 2016, the cost coverage for market dominant International Ancillary Services was slightly (less than one percent) below 100 percent. *See* Table IV-2. As the Postal Service explains, the situation was due to the failure of Inbound Registered Mail to cover its costs. FY 2016 ACR at 62. In FY 2015, Inbound Registered Mail had a positive contribution of $19.5 million, but in FY 2016, after the reassignment of delivery costs from Inbound Letter Post, already lost $9.8 million.[39] *Id*. at 62. As discussed in Section IV.B above, Inbound Letter Post has traditionally been an underwater product. The Postal Service, however, anticipates that in 2017-2018, the cost coverage for Inbound Registered Mail will exceed 100 percent after implementation of a number of currently proposed measures. *Id.* at 62-63. The Public Representative suggests close monitoring of the impact of the anticipated measures on the cost coverage for Inbound Registered Mail.

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[39] *See also* Library Reference USPS-FY15-NP2, file “Reports (Unified)”, tab ‘A Pages (md)’.

V. WORKSHARING

A. Introduction

39 U.S.C. §3622(e)(2) directs the Commission to ensure worksharing discounts do not exceed the costs avoided by the Postal Service. The Public Representative's comments focus on thirty-three First-Class Mail, Standard Mail, and Package Services worksharing passthroughs that exceed 100 percent.

As the Public Representative suggested in his FY 2015 comments, the Commission should require the Postal Service to improve the substance of its justifications under the statutory exception which allow greater than 100 percent passthroughs.[40] The Public Representative considers the exceptions listed under (A) new postal service, (B) rate shock, and (D) efficiency to be more temporary in nature.[41] However, it appears that the Postal Service often abuses this temporary status by reusing the same exceptions year-after-year for the same product categories (especially the rate shock exception). To prevent potential abuse, the Public Representative suggests that the Postal Service submit a plan detailing how, over a limited number of rate cycles, it intends to bring presumptively excessive passthroughs under 100 percent.

The Postal Service continues to not justify many excessive passthroughs due to the systemic timing problem of aligning discounts with cost avoidance data for the purposes of the ACD. Technically, this leads to a conclusion that the associated passthroughs are out of compliance, even though the problem is well understood. The Public Representative suggests this is an issue that the Commission may choose to examine during the 10-year review.

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[40] FY 2015 Public Representative Comments at 42; *see* 39 U.S.C. § 3622(e)(2).

[41] The Public Representative considers (C) educational, cultural, scientific, or informational value to be more permanent in nature (and does not discuss them in its comments).

B. First-Class Mail

Seven First-Class Mail passthroughs exceed 100 percent. *See* Table V-1.

Table V-1
First-Class Mail
Problematic Passthroughs — FY 2016

Category	Passthrough (%)	USPS Statutory Justification	Public Representative's Conclusion
First-Class Mail			
Presorted Letters/Cards			
Automation AADC Letters	111.1	None	Non-compliant
Automation Mixed AADC Cards	183.3	None	Non-compliant
Automation AADC Cards	150.0	None	Non-compliant
Automation 5-Digit Cards	118.2	None	Non-compliant
Flats			
Automation ADC Flats	109.6	None	Non-compliant
Automation 3-Digit Flats	102.6	None	Non-compliant
Automation 5-Digit Flats	161.3	Rate Shock	Non-compliant

Data Source: FY 2016 ACR at 14-21.

Four First-Class Mail Presorted Letters/Card passthroughs exceed 100 percent: Automation AADC Letters, Automation Mixed AADC Cards, Automation AADC Cards, and Automation 5-Digit Cards. The Postal Service does not justify these excessive passthroughs on statutory grounds, but states that it will either fix the passthroughs in the next annual market dominant price increase or cite to a statutory exception. FY 2016 ACR at 15-18. The Public Representative concludes that the passthroughs for these products are not in compliance with §3622(e)(2).

Three First-Class Mail Flats passthroughs exceed 100 percent: Automation ADC Flats, Automation 3-Digit Flats, and Automation 5-Digit Flats. The Postal Service did not provide a statutory exemption for the excessive passthroughs for Automation ADC Flats and Automation 3-Digit Flats. The Public Representative concludes that the passthroughs for these products are not in compliance with §3622(e)(2).

The Postal Service maintains that bringing the 161.3 percent passthrough for Automation 5-Digit Flats into compliance "would require up to a 16.7 percent price increase (or a 10.3 percent price decrease)." FY 2016 ACR at 21. Thus, the Postal Service attempts to justify this passthrough using the rate shock exception. *See* §3622(e)(2)(B).

The Public Representative notes that part of the rate shock exception specifies that the discount will be phased out over time. *See* §3622(e)(2)(B)(i). The history of this discount does not support a demonstration of any attempt to phase out this discount over time. *See* Table V-2.

Table V-2
History of First-Class Mail
Automation 5-Digit Flats Passthroughs

Year	Passthrough (%)	Cost Avoidance (¢)	Discount (¢)	Excess (¢)
FY 2013	133.3	14.1	18.8	4.7
FY 2014	120.4	15.2	18.3	3.1
FY 2015	120.8	15.9	19.2	3.3
FY 2016	161.3	11.9	19.2	7.3

Data Source: FY 2016 ACR at 20.

From FY 2013 through FY 2016, the discounts have ranged from 18.3 to 19.2 cents, while the cost avoidances have ranged from 11.9 to 15.9 cents. There is no evidence of any attempt to phase out the excessive discount in this time period. Therefore, the Public Representative contends that the requirements for the rate shock exception have not been met and the passthrough is not in compliance with the statute.

Furthermore as noted in the Public FY 2015 Representative Comments, the Postal Service also has the option of building in a buffer and passing through less than 100 percent of costs avoided. This is one method of addressing the Postal Service's "volatility of cost avoidance estimates" concern. *See* FY 2015 Public Representative Comments at 45.

C. Standard Mail

Nineteen Standard Mail passthroughs exceed 100 percent. *See* Table V-3.

Table V-3
Standard Mail
Non-ECSI, Problematic Passthroughs — FY 2016

Category	Passthrough (%)	USPS Statutory Justification	Public Representative's Conclusion
Standard Mail (Commercial and Nonprofit)			
Letters			
Automation Mixed AADC Letters	800.0	Efficiency	Non-compliant
Automation AADC Letters	121.4	Rate Shock	Non-compliant
Non-automation 3-Digit Non-Machinable Letters	113.0	None	Non-Compliant
Non-automation 5-Digit Non-Machinable Letters	125.4	Rate Shock	Non-Compliant
DNDC Dropship Letters	175.0	Rate Shock	Non-compliant
DSCF Dropship Letters	191.3	Rate Shock	Non-compliant
Flats			
Automation FSS Non-scheme	176.6	To Be Eliminated	Non-Compliant
Automation FSS Scheme	333.3	To Be Eliminated	Non-Compliant
Pre-barcoding Automation Mixed ADC Flats	241.2	Efficiency	Non-Compliant
Non-automation FSS Non-scheme	175.0	To Be Eliminated	Non-Compliant
Parcels			
NDC Irregular Parcels	133.6	None	Non-compliant
NDC Marketing Parcels	115.9	Efficiency	Non-Compliant
Mixed NDC Machinable Barcoded Parcels	164.9	Efficiency	Non-Compliant
Mixed NDC Irregular Barcoded Parcels	164.9	Efficiency	Non-Compliant
Mixed NDC Barcoded Marketing Parcels	164.9	Efficiency	Non-Compliant
Carrier Route Letters			
DNDC Letters	160.0	Rate Shock	Non-Compliant
DSCF Letters	187.0	Rate Shock	Non-compliant
High Density and Saturation Letters			
DNDC Letters	160.0	Rate Shock	Non-compliant
DSCF Letters	187.0	Rate Shock	Non-compliant

Data Source: FY 2016 ACR at 38-49 (Revised on January 31, 2017).

The Postal Service is eliminating three of the rate categories with passthroughs in excess of 100 percent; Flats-Automation FSS Non-scheme, Automation FSS Scheme, and Non-automation FSS Non-scheme. The Public Representative concludes that the passthroughs for these products are not in compliance with §3622(e)(2).

However, since the categories are being eliminated, no further corrective action is necessary.

The Postal Service did not provide a statutory exception for the excessive passthroughs for two rate categories: Non-automation 3-Digit Non-Machinable Letters, and NDC Irregular Parcels. The Public Representative concludes that the passthroughs for these products are not in compliance with §3622(e)(2).

For the remaining fourteen rate categories, the Postal Service justifies the excessive discounts using either the rate shock (§3622(e)(2)(B)) or the efficiency (§3622(e)(2)(D)) exceptions. These same fourteen rate categories exhibited excessive passthroughs in FY 2015. In some instances, the justifications for the excessive passthrough have changed. However, the Public Representative's position is that excessive passthroughs justified under the rate shock or the efficiency exceptions should be phased out over time. The Public Representative is not persuaded that the Postal Service has a plan for ever purposefully correcting these discrepancies. Therefore, the Public Representative concludes that the passthroughs for these rate categories are not justified under the rate shock or the efficiency exceptions, and do not comply with the requirements of §3622(e)(2).

The Public Representative also notes that the magnitude of the rate change necessary to bring all of the rate shock justified categories into compliance range from 0.3 cents to 2.1 cents. Assuming that a rate shock argument is persuasive, the lower magnitude rate changes could be corrected immediately, while the higher magnitude rate changes could be corrected over one or two rate adjustment cycles.

D. Package Services

Seven Package Service, Bound Printed Matter, passthroughs exceed 100 percent.[42] *See* Table V-4. The Postal Service does not provide a statutory justification for any of the excessive passthroughs. It does state that the passthroughs will be adjusted in the next general market dominant rate change. FY 2016 ACR at 56-60.

Table V-4
Package Services
Non-ECSI, Problematic Passthroughs — FY 2016

Category	Passthrough (%)	USPS Statutory Justification	Public Representative's Conclusion
Package Services			
Bound Printed Matter Dropship Flats			
Basic, Carrier Route DNDC Flats	113.7	None	Non-compliant
Basic, Carrier Route DSCF Flats	106.4	None	Non-compliant
Basic, DFSS Flats	108.2	None	Non-compliant
Basic, Carrier Route DDU Flats	106.5	None	Non-compliant
Bound Printed Matter Dropship Parcels			
Basic, Carrier Route DNDC Parcels/IPPs	113.7	None	Non-compliant
Basic, Carrier Route DSCF Parcels/IPPs	110.6	None	Non-compliant
Basic, Carrier Route DDU Parcels/IPPs	111.1	None	Non-compliant

Data Source: FY 2016 ACR at 56-60.

The Public Representative concludes that the passthroughs for the above Package Service, Bound Printed Matter, categories are out of compliance.

[42] Note that two passthroughs within Media Mail/Library Mail also exceeded 100 percent but were adequately justified using the educational, cultural, scientific, or informational value (ECSI) exception. *See* 39 U.S.C. § 3622(e)(2)(C).

VI. COMPETITIVE PRODUCTS

A. Introduction

As mandated by 39 U.S.C. § 3633(a), the Commission's regulations in 39 C.F.R. § 3015.7 require that:

- Market dominant products do not subsidize competitive products (39 U.S.C. § 3633(a)(1));
- Each competitive product covers its attributable costs (39 U.S.C. § 3633(a)(2)); and
- Competitive products collectively cover an appropriate share of the Postal Service's institutional costs (39 U.S.C. § 3633(a)(3)).

The Public Representative concludes that market dominant products do not subsidize competitive products in accordance with 39 U.S.C. § 3633(a)(1). A number of competitive products and services, however, did not cover attributable costs in violation of 39 U.S.C. § 3633(a)(2). These products include, but are not limited to International Money Transfer Service–Inbound and Outbound, Inbound Air Parcel Post (at non-UPU rates) and Outbound International Insurance. Also, in the FY 2016 ACR the Postal Service identified a number of Negotiated Service Agreements (NSAs) that did not cover costs. FY 2016 ACR at 86-87, 89. The analysis of cost coverage for these products and services follows. The Public Representative, however, acknowledges that Inbound Parcel Post (at UPU rates) covered its costs in FY 2016, after being underwater in FY 2015. FY 2015 ACD at 86-87. Furthermore, in FY 2015-2016, the Postal Service implemented several rate increases, which appear to have had a positive impact on the cost coverage.[43] The Public Representative concludes that competitive products collectively cover an appropriate share of the Postal Service's institutional costs in accordance with 39 U.S.C. § 3633(a)(3).

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[43] *See* Docket No. CP2015-24, Order Accepting Changes in Rates for Inbound Parcel Post (at UPU Rates), December 29, 2014 (Order No. 2160); Docket No. CP2016-9, Order Approving Changes in Rates of General Applicability for Competitive Products, November 13, 2016. (Order No. 2814).

B. Market Dominant Products Did Not Subsidize Competitive Products

In order to test for compliance with 39 U.S.C. § 3633(a)(1), the Public Representative applies the cross-subsidy test set forth in 39 C.F.R. § 3015.7(a). In Order No. 399, the Commission approved the hybrid incremental cost methodology for this test.[44] Under that methodology, incremental costs for domestic competitive products, attributable costs for competitive international products, and group specific costs are aggregated to calculate the hybrid incremental cost total for competitive products. To satisfy the cross-subsidy test, and comply with 39 U.S.C. § 3633(a)(1), the total hybrid incremental costs for competitive products must be lower than the total revenue for competitive products.

In FY 2016, the total hybrid incremental costs for competitive products were $12.791 billion.[45] FY 2016 ACR at 84. In FY 2016, the total revenue for competitive products (Competitive Mail and Services) was $18.495 billion. *Id.* In FY 2016, the total competitive products revenue exceeds the total hybrid incremental costs for competitive products. The Public Representative concludes that the cross-subsidy test is satisfied, and market dominant products did not subsidize competitive products during FY 2016.

However, questions remain concerning the accuracy of the above methodology employed in calculation of the total hybrid incremental costs. In the recent Order No. 3506, the Commission confirmed that the incremental cost test “effectively” and “precisely” tests for cross-subsidy, but emphasized that it would “now interpret attributable costs to mean the incremental costs of a class or a product.” Order No. 3506 at 58, 60. In Order No. 3641, the Postal Service adopted a revision to 39 C.F.R. 3015.7 (b) as follows: “Pursuant to 39 U.S.C. 3631(b), the Commission will calculate a competitive product's attributable costs as the sum of its volume-variable costs, product-specific costs, and those *inframarginal costs* calculated as part of a competitive

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[44] Docket No. RM2010-4, Order Accepting Analytical Principles Used in Periodic Reporting (Proposal Twenty-Two through Twenty-Five), January 27, 2010, at 4-5 (Order No. 399).

[45] *See* also Library Reference USPS-FY16-1, file “Public_FY16CRAReport”, tab ‘Cost3’.

product's incremental costs." (Emphasis added). Order No. 3641 at 11. As defined in 39 C.F.R. § 3015.7(a), to test for cross subsidy, using the incremental test, but "[t]o the extent that incremental cost data are unavailable, the Commission will use the sum of competitive product's volume variable costs and product specific costs supplemented to include causally related group-specific costs to test for cross-subsidies." Order No. 3641 at 13.

In the FY 2016 ACR, the Postal Service describes challenges it encountered attempting to estimate the incremental and inframarginal costs, as requested in the Commission Orders Nos. 3506 and 3641. FY 2016 ACR at 4-6. The Public Representative agrees that time constraints and other described obstacles could preclude the Postal Service from further developing "the incremental cost estimation model"…"using the *adjusted* volume variable costs as the inputs into the incremental cost estimation model." *Id.* at 5. The Public Representative also appreciates the provision of the additional materials associated with the incremental costs (and not available in prior years ACRs), which increases transparency. *Id.* at 7-8. The Public Representative however, encourages the Postal Service to consider further development of the incremental cost model in the light of the changes in costing methodology set up by Order No. 3641.

C. Competitive Products That Did Not Cover Attributable Costs

1. International Money Transfer Service (IMTS) –Inbound and International Money Transfer Service–Outbound

In FY 2010, the Commission approved the Postal Service's request to classify International Money Transfer Service–Inbound, and International Money Transfer

Service–Outbound as two separate competitive products.[46] In FY 2016 (as in FY 2014 and FY 2015), both these products failed to cover attributable costs.[47]

In the FY 2014 ACD, the Commission concluded that both the International Money Transfer Service–Inbound, and International Money Transfer Service–Outbound products failed to satisfy 39 U.S.C. § 3633(a)(2), and ordered the Postal Service to take corrective action. FY 2014 ACD at 71. The Commission also suggested considering the option of a price increase for International Money Transfer Service–Outbound. *Id.* at 76. In its responses to the Commission's FY 2014 and FY 2015 ACD requests, the Postal Service discussed the major difficulties in improving the reliability of the International Money Transfer Service cost estimates, and emphasized the small number of International Money Transfer Service transactions.[48] In the FY 2016 ACR, the Postal Service confirms that it "has taken mitigation steps" to address the cost coverage of IMTS-Outbound, and its rates will be increased substantially effective January 22, 2017.[49] FY 2016 ACR at 88. The Postal Service cites to Order No. 3622 that states: "this price increase should generate sufficient revenue to cover the attributable costs for Outbound IMTS." FY 2016 ACR at 88, *citing* Order No. 3622 at 8. In January of last year, the Postal Service also implemented a price increase for IMTS–Outbound.[50] In FY 2016, the product revenue increased, but the cost coverage was still below 100

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[46] *See* Docket No. MC2009-19, Order Approving Addition of Postal Services to the Mail Classification Schedule Products Lists, January 13, 2010 (Order No. 391).

[47] *See* FY 2016 ACR at 86; FY 2015 ACD at 84-85; FY 2014 ACD at 71.

[48] See FY 2014 ACR, Responses of the United States Postal Service to Commission Requests for Additional Information Regarding IMTS and EPG in the FY 2014 Annual Compliance Determination, Question 4, June 30, 2015; FY 2015 ACR, Second Response of the United States Postal Service to Commission Requests for Additional Information in the FY 2015 Annual Compliance Determination, Question 2, June 27, 2016.

[49] The average price increase for International Ancillary Services is 10.6 percent, but for some services the increase will be higher. Thus, for International Postal Money Order fees (which is a part of IMTS-Outbound), the price increase is 73.7 percent. *See* FY 2016 ACR at 88; Docket No. CP2017-20, Order Approving Price Adjustments for Competitive Product, November 18, 2016 at 8 (Order No. 3622).

[50] *See* Docket No. CP2016-9, Order Approving Changes in Rates of General Applicability for Competitive Products, November 13, 2016, at 3 (Order No. 2814).

percent. The Public Representative concludes that an additional price increase effective January 22, 2017, should have a positive impact on International Money Transfer Service cost coverage in FY 2017.

2. Inbound Air Parcel Post (at non-UPU rates)

Prior to July 1, 2016, Inbound Air Parcel Post (at non-UPU rates), consisted of inbound air parcels for Royal Mail and collectively for several European postal operators that are parties to the E-Parcel Group (EPG) Agreement. FY 2016 ACR at 87. In FY 2012-2015, Inbound Air Parcel Post (at non-UPU rates) failed to cover attributable costs. *See* FY 2015 ACD at 90; FY 2014 ACD at 79; FY 2013 ACD at 90; FY 2012 ACD at 170. In the FY 2015 ACR, in response to the Commission prior year directives to improve the product's financial results or extricate itself from the Agreement, the Postal Service confirmed that it was "taking remedial measures to address Inbound Air Parcel Post at Non-UPU Rates," tendered by several postal operators and would exit the EPG agreement according to its terms on June 30, 2016." FY 2015 ACR at 67. *See also* FY 2014 ACD at 81.

In its FY2016 ACR, the Postal Service confirms that it exited the EPG agreement as intended, and after June 30, 2016, the only remaining agreement in the Inbound Air Parcel Post (at Non-UPU rates) grouping that continued to be operative was a negotiated service agreement with Royal Mail. FY 2016 ACR at 87-88. Considering that Royal Mail agreement covered its costs in FY 2016, the Public Representative concludes that the performed action was appropriate.[51]

[51] *See* Library Reference USPS-FY16-NP2 (Revised January 19, 2017), file "NSA Summary (Unified)", tab 'Summary ICRA16'.

3. Inbound Competitive Multi-Service Agreements with Foreign Postal Operators 1

In the FY 2015 ACD, the Commission found that the Inbound Competitive Multi-Service Agreements with Foreign Postal Operators 1 (that consisted of nine bilateral NSAs) satisfied 39 U.S.C. § 3633(a)(2) "because revenue exceeded attributable costs for each [NSA]." FY 2015 ACR at 92. In FY 2016, one of the agreements failed to cover costs, which raises a concern regarding its compliance with 39 U.S.C. § 3633(a)(2). FY 2016 ACR at 89. The Postal Service intends to replace the rates for the agreement so that they "provide adequate cost coverage." *Id.* Also, considering that the FY 2016 cost coverage was just slightly below 100 percent, the Public Representative expresses hope that the rate change will allow the agreement to cover its costs.[52]

4. Outbound International Insurance

The Postal Service notes that the insurance fees for both Priority Mail International and Priority Mail Express International will be raised effective January 22, 2017. FY 2016 ACR at 89. The Postal Service affirms that if the product continues to underperform, "management will propose further remedial measures for consideration." *Id.* at 89. Considering that Outbound International Insurance covered its costs in FY 2015, the Public Representative concludes that the proposed approach is reasonable.

5. Domestic NSA Contracts That Did Not Cover Attributable Costs

In FY 2016, in comparison with the previous years, the number of competitive NSAs that did not cover costs increased significantly.[53] In the FY 2016 ACR, the Postal

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[52] *See* Library Reference USPS-FY16-NP2 (Revised January 19, 2017), file "NSA Summary (Unified)", tab 'Summary ICRA16'.

[53] In FY 2015 there were two or less NSAs that failed to cover costs. *See* FY 2015 ACD at 81; FY 2014 ACD at 73.

Service identified 13 domestic NSAs that did not cover costs. FY 2016 ACR at 86-87. As the Postal Service reports, failure to cover costs was to a large extent "due to significant changes (deterioration) in actual profile." Such changes primarily include a shift towards mail pieces that are either lighter or destinated to a closer zone. *Id.* Considering a rapid increase in a number of domestic competitive NSAs, the Public Representative suggests that when evaluating the proposed cost coverage, the Postal Service perform an additional sensitivity analysis. This may help to ensure that changes in profile do not result in cost coverages falling below 100 percent. The Public Representative also suggests that the Postal Service perform its comprehensive evaluation of the contracts that failed to cover costs in FY 2016, and either amend or terminate the underperforming contracts.

D. Competitive Products Collectively Covered an Appropriate Share of the Postal Service's Institutional Costs

Competitive products must cover "an appropriate share of the institutional costs of the Postal Service." 39 U.S.C. § 3633(a)(3). The Commission has determined "the appropriate share of the institutional costs to be recovered from competitive products collectively is, at a minimum, 5.5 percent of the Postal Service's total institutional costs."[54] 39 C.F.R. § 3015.7(c).

In FY 2016, the Postal Service's total institutional costs were $36.363 billion; 5.5 percent of which would be approximately $2.0 billion.[55] Competitive products provided a contribution of $5.999 billion in FY 2016, and thereby satisfy the requirements of 39 U.S.C. § 3633(a)(3) and 39 C.F.R. § 3015.7(c). *Id.*

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[54] In Order No, 3624, the Commission initiated an examination of the appropriateness of the current 5.5 contribution level for competitive products. *See* Docket No. RM2017-1, Advance Notice of Proposed Rulemaking to Evaluate the Institutional Cost Contribution Requirement for Competitive Products, November 22, 2016 (Order No. 3624). The docket is currently pending before the Commission.

[55] Library Reference USPS-FY16-1, file "Public_F16CRAReport", tab 'Cost3'. *See also* FY 2016 ACR at 89-90.

VII. CONCLUSION

The Public Representative respectively submits the foregoing comments for the Commission's consideration.

Respectfully submitted,

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